No.

OFFICE OF THE CLERK

In The

Supreme Court of the United States

October Term, 1993

JAMES W. BURKE, as Personal Representative of the ESTATE OF EDNA SPROULL WILLIAMS, Deceased,

Petitioner,

vs.

THE UNITED STATES,

Respondent.

Petition for Writ of Certiorari to the United States Court of Appeals for the Federal Circuit

PETITION FOR WRIT OF CERTIORARI

WILLIAM R. FRAZIER
Counsel of Record
FRAZIER & FRAZIER
Attorneys for Petitioner
1515 Riverside Avenue
Suite A
Jacksonville, Florida 32204
(904) 353-5616

1705
Lutz Appellate Services, inc.
(800) 3 APPEAL • (800) 5 APPEAL • (800) BRIEF 21

'16 pd

QUESTION PRESENTED

Whether or not a charitable deduction for federal estate tax purposes, allowed by § 2055(a) of the Internal Revenue Code must be reduced by the amount of certain administrative expenses paid by the decedent's personal representative from post-mortem income, notwithstanding the fact that the estate tax charitable deduction claimed on the estate's estate tax return, Form 706, in the amount of $8,869,080.10, in a situation wherein the charitable institution actually received assets of the estate in payment of the charitable bequest, in excess of $10,091,707.94.

The administrative expenses in question amounted to the sum of $144,441.

The Commissioner of Internal Revenue in auditing the estate's federal estate tax return determined that the charitable bequest should be reduced by the amount of the administrative expenses although paid from post mortem income, plus estate taxes attributable thereto or a reduction in the estate's charitable deduction as claimed of $288,258.94. The action of the Commissioner, resulted in an estate tax deficiency in the amount of $80,110.87, plus accrued interest in the amount of $30,606.13, or a total liability of $110,717.00, which gave rise to this litigation.

PARTIES TO THE PROCEEDING

The full names of every party or the names of all parties to this case appear in the caption of the case.

TABLE OF CONTENTS

	Page
Question Presented	i
Parties to the Proceeding	ii
Table of Contents	iii
Table of Citations	iii
Opinions Below	1
Grounds of Jurisdiction	2
Statute Involved	2
Statement of the Case	2
Statement of Jurisdiction	9
Reasons for Granting the Writ	9
Conclusion	16

TABLE OF CITATIONS

Cases Cited:

Estate of Dorothy J. Warren, Dec. v. Commissioner of Internal Revenue, 981 F.2d 776 (5th Cir. 1993) 9, 10, 11

Estate of Edward H. Luehrmann v. Commissioner, 287 F.2d 10 (8th Cir. 1961) 12

Contents

Page

Estate of Gordon P. Street v. Commissioner, T.C. Memo 1988-553, 56 TCM 774 (1988) 14, 15

Estate of Harry E. Wright, Jr. v. United States, 677 F.2d 53 (9th Cir. 1982) 13

Estate of Walter E. Richardson v. Commissioner, 89 T.C. 1193 (1987) 14

Harrison v. Northern Trust Co., et al., 317 U.S. 476 (1943) 11, 12, 13

Heim v. Nee, 40 F. Supp. 594 (W.D. Mo. 1937) 12

In Re: Sage's Estate, 122 F.2d 480 (3rd Cir. 1941) 13

William J. Oetting, Exec. v. United States, 712 F.2d 358 (8th Cir. 1983) 13

Statutes Cited:

28 U.S.C. § 1254 2

28 U.S.C. § 1295(a)(3) 9

28 U.S.C. § 1491 9

Internal Revenue Code:

§ 501(c)(3) 3

Contents

	Page
§ 2053	6
§ 2054	6
§ 2055	11, 13, 15
§ 2055(a)	i, 2
§ 2056	13
§ 2056(a)	14, 15

Other Authority Cited:

Treasury Regulations § 1.642(g)-1	6

APPENDIX

Appendix A — Judgment of the United States Court of Appeals for the Federal Circuit Dated June 2, 1993 ... 1a

Appendix B — Opinion of the United States Court of Appeals for the Federal Circuit Dated June 2, 1993 ... 3a

Appendix C — Opinion of the United States Court of Appeals for the Federal Circuit Dated June 2, 1993 ... 18a

Appendix D — Decision of the United States Court of Appeals for the Fifth Circuit in the Case of *Estate of Dorothy J. Warren, Deceased, et al. v. Commissioner of Internal Revenue* Dated January 13, 1993 ..... 20a

Contents

Page

Appendix E — Judgment of the United States Claims Court Filed November 29, 1991 ..... 40a

Appendix F — Order of the United States Claims Court Filed November 27, 1991 ..... 41a

Appendix G — Internal Revenue Code Section 2055(a) .. 52a

No.

In The

Supreme Court of the United States

October Term, 1993

JAMES W. BURKE, as Personal Representative of the ESTATE OF EDNA SPROULL WILLIAMS, Deceased,

Petitioner,

vs.

THE UNITED STATES,

Respondent.

Petition for Writ of Certiorari to the United States Court of Appeals for the Federal Circuit

PETITION FOR WRIT OF CERTIORARI

Petitioner prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Federal Circuit entered in the above-entitled cause on June 2, 1993.

OPINIONS BELOW

The opinion of the United States Claims Court in Docket No. 540-89T entered November 27, 1991, is not officially reported and a copy of the Claims Court opinion is reproduced in Appendix F, *infra* p. 41a.

The opinion of the United States Court of Appeals for the Federal Circuit in Docket No. 92-5062 entered June 2, 1993, is likewise not officially reported and a copy of the Court of Appeals opinion is reproduced as Appendix B, *infra* p. 3a.

GROUNDS OF JURISDICTION

(i) The judgment of the United States Court of Appeals for the Federal Circuit sought to be reviewed herein was entered on June 2, 1993 (Appendix A, *infra* p. 1a).

(ii) There was no motion filed in the case for a rehearing, and no application for extension of time within which to file the petition for writ of certiorari was filed.

(iii) The statutory provision believed to confer on this Court jurisdiction and review judgment by writ of certiorari is Title 28 U.S.C. § 1254.

STATUTE INVOLVED

The statutory provision involved is § 2055(a) of the Internal Revenue Code which is set forth in Appendix G, *infra* p. 52a .

STATEMENT OF THE CASE

Edna Sproull Williams died testate on February 28, 1982, while a resident of Jacksonville, Florida.

The decedent died testate leaving a Will dated October 9, 1979, and a Codicil thereto dated October 30, 1979.

Decedent's Will and Codicil were filed for probate in the Circuit Court for Duval County, Florida, on March 2, 1982.

James W. Burke, the petitioner in this case, is the surviving and presently acting Personal Representative of the decedent's estate.

The Edna Sproull Williams Foundation was created during decedent's lifetime pursuant to the terms of a charitable trust agreement dated February 13, 1976, and is an organization exempt from taxation under § 501(c)(3) of the Internal Revenue Code.

Article I of the decedent's Will provided in part as follows:

> . . . I direct that all estate, inheritance, and succession taxes that may be levied against my estate, including such taxes levied against property constituting any part of my estate for federal estate tax purposes, whether passing under this Will or otherwise, shall be paid by my Personal Representatives, solely out of the residuary estate being bequeathed hereunder, it being my intention that the portion of my estate devised and bequeathed to or for the benefit of all legatees hereunder, except the residuary legatee, shall be enjoyed by them free from any burden from such taxes . . . .

The decedent bequeathed her residuary estate under Article XIII of her Will providing in part:

> I give, devise and bequeath all the rest, residue and remainder of my estate, including all lapsed legacies or devises, after paying therefrom any debts and taxes, including estate, inheritance, or succession taxes and other obligations of my estate, including all administrative expenses, to the Trustees of the

> Edna Sproull Williams Foundation which I established under a Trust Agreement dated February 13, 1976 . . . .

The Personal Representatives of the decedent's estate filed the estate's United States Estate Tax Return, Form 706, dated November 24, 1982, within the time and manner prescribed by law.

An amended United States estate tax return dated February 21, 1983, was filed, for the purpose of correcting the calculation of the credit for State death taxes.

On November 11, 1982, and prior to the filing of the federal estate tax return, the Personal Representatives of the decedent's estate filed a petition for construction of the decedent's Will in the Circuit Court for Duval County, Florida, seeking a construction of Article I and Article XIII of the decedent's Will, and the entry of an order of court authorizing the petitioners as personal representatives of the decedent's estate to pay administrative expenses out of the income earned over a period of years while the estate remained open, rather than paying these expenses out of and as a charge against the principal of the decedent's residuary estate.

In the petition for construction of the Will, the petitioners pointed out to the court that under Article I of the Will there was a direction that all estate taxes were to be paid by the Personal Representatives solely out of the residuary estate, but that Article I gave no specific directions with regard to payment of administrative expenses.

The petition for construction of Will also called the attention of the court to Article XIII of the decedent's Will that provided for the bequest of her residuary estate to the Edna Sproull Williams Foundation after the payment therefrom of any debts and taxes, including estate taxes and other obligations of the estate, including all administrative expenses.

The petitioners also pointed out to the court that while Article I of the Will mandated that estate taxes be paid out of the residuary estate, Article XIII implied no such mandate with respect to administrative expenses, and petitioners urged the court to interpret this portion of the decedent's Will to mean that such expenses may be paid out of such residuary estate, at the discretion of the Personal Representatives, if not paid out of income. Petitioners further pointed out that if decedent had intended administrative expenses to be paid out of the residuary estate as an absolute requirement, administrative expenses would have been included with estate taxes as mandated by Article I of the Will.

The court entered its order pursuant to the petition on November 12, 1982, in which it was ordered as follows:

> Articles I and XIII of the decedent's Will are construed to authorize payment of the administrative expenses by the Personal Representatives out of income if they choose to pay such expenses out of income, and to the extent that the Personal Representatives do not choose to pay administrative expenses out of income, such administrative expenses shall be paid out of the residuary share of the estate prior to distribution to the residual beneficiary, as requested in the Petition.

The Personal Representatives, in filing the estate tax return (Form 706), did not take a deduction for any of the estate's administrative expenses.

The Personal Representatives, in filing the first fiduciary income tax return for the decedent's estate covering the period March 1, 1982, through December 31, 1982, deducted administrative expenses totalling $144,441 consisting of fiduciary

fees of $75,000, attorneys' and accountants' fees $51,765, and other miscellaneous administrative deductions totalling $17,676.

At the time the fiduciary income tax return was filed, the Personal Representatives filed the elective statement required by the Treasury Regulations § 1.642(g)-1 in which the estate waived the right to deduct these administrative expenses as deductions from the decedent's gross estate for estate tax purposes under §§ 2053 or 2054 of the Internal Revenue Code.

The decedent's estate tax return shows a total gross estate of $10,489,753.94, from which total allowable deductions were taken of $9,747,444.42, leaving a taxable estate of $742,309.52.

The return further disclosed that of the total deductions claimed of $9,747,444.42, $9,662,605.10 represented deductions for charitable bequests of which $8,869,080.10 represented the residual bequest made by the decedent's Will to the Trustees of the Edna Sproull Williams Foundation.

The Commissioner in auditing the federal estate tax return determined that the administrative expenses in the amount of $144,441 which had been claimed as expenses on the estate's fiduciary income tax return, Form 1041, reduced the amount of the charitable bequest made to the Foundation.

The Commissioner actually reduced the amount of the charitable deduction resulting from the gift to the Foundation by $236,536.38 which was represented by the $144,441 of administrative expenses and the estate taxes attributable thereto, with the result that the Commissioner assessed a deficiency in estate tax against the decedent's estate of $80,110.87.

The Personal Representatives paid the deficiency in the amount of $80,110.87, plus interest in the amount of $30,606.13, in full under protest on or about July 9, 1985.

Within the time and manner prescribed by law, the Personal Representatives filed a claim for refund, Treasury Form 843, seeking a refund of the $80,110.87 deficiency, plus the interest paid, which claim was disallowed on October 7, 1987. Petitioner filed his complaint in the United States Court of Claims on October 4, 1989 (petitioner's complaint and copy of Treasury Form 843 attached thereto, and respondent's answer, paragraph 13, page 2).

The $144,441 of administrative expenses in question were paid during the calendar year 1982 by the Personal Representatives of the decedent's estate solely from the income accumulated during the first ten months of the estate's administration and from no other source.

During the first ten months of the administration of the decedent's estate ending December 31, 1982, the total income from all sources amounted to $434,514.78 and that expenses were disbursed from this income, including the $144,441 in question in this case which left net accumulated income of the estate as of December 31, 1982 of $288,258.94.

Distributions of assets and property were made from the estate of Edna Sproull Williams, deceased, to the Trustees of the Edna Sproull Williams Foundation from the inception of the administration of the decedent's estate through December 31, 1989, as follows:

Year	Amount
1982	$ 696,924.18
1983	5,043,338.74
1984	531,686.48
1985	619,758.54
1986	600,000.00
1987	1,900,000.00

Year	Amount
1988	-0-
1989	700,000.00
Total:	$ 10,091,707.94

to which was added $312,316.99 unrealized appreciation on securities at date of transfer and $151,268.35 of accrued interest at date of transfer, resulting in total value of assets transferred to the Foundation during said period of $10,555,293.28.

The case was heard before the United States Claims Court on Motions and Cross-Motions for Summary Judgment filed by the parties together with supporting exhibits, affidavits, etc., therefore, no trial or hearing was held before the Trial Court.

The Trial Court upheld the Commissioner's determination and entered a final judgment in this case on November 29, 1991.

The Trial Court held that under the Florida Statute and under the terms of the decedent's Will the administrative costs in question were to be charged against the principal of the estate. The Court therefore concluded that this reduced the amount of the residue to be received by the charitable foundation under the terms of the decedent's Will. Therefore the Court held that the estate's charitable deduction must be reduced by the amount of these administrative expenses.

For obvious reasons, we believe this conclusion erroneous, as a matter of law.

Following the entry of the Trial Court's final judgment in this case a notice of appeal was filed and appeal taken and prosecuted before the United States Court of Appeals for the Federal Circuit.

The Court of Appeals upheld the decision of the Trial Court. The Appeals Court entered a final judgment in this case on June 2, 1993. This petition was filed within the ninety day period prescribed by Rule 13 of the Rules of the Supreme Court.

STATEMENT OF JURISDICTION

(a) The statutory basis for jurisdiction of the Trial Court (United States Claims Court) is Title 28 U.S.C. § 1491.

(b) The statutory basis for jurisdiction of the United States Court of Appeals for the Federal Circuit, hearing the appeal from the adverse decision of the Trial Court is Title 28 U.S.C. § 1295(a)(3).

REASONS FOR GRANTING THE WRIT

1. The decision of the United States Court of Appeals for the Federal Circuit is in direct conflict with the recent decision of the United States Court of Appeals for the Fifth Circuit in *Estate of Dorothy J. Warren, Dec. v. Commissioner of Internal Revenue*, 981 F.2d 776 (5th Cir. 1993) (Appendix D, *infra* p. 20a), reversing and remanding the decision of the United States Tax Court, T.C. Memo 1990-377, 60 TCM 206 (1990). The Court of Appeals for the Fifth Circuit held in a similar estate tax deduction case, involving charitable transfers, that 72 1/2 percent of the expenses that were charged to the estates post mortem income did not reduce the amount of the estate's charitable deduction for federal estate tax purposes. The court so held although the decedent's Will provided that all administrative expenses were to be paid from the residuary estate. The court further held that the state court decree was binding and that the estate tax charitable deduction must be computed on the basis of what the charities received under the Will pursuant to the state court decree.

In the *Warren* case, the Commissioner of Internal Revenue contended and the Tax Court agreed that the will required that all administrative expenses be charged to the residuary corpus before computing " . . . the initial net fair market value of the assets constituting the trust."

2. The Court of Appeals for the Federal Circuit, toward the end of its opinion, seems to agree that the *Warren* case is in conflict with their opinion in this case, as it relates to the issue of reducing the charitable deduction by the amount of administrative expenses paid from post-mortem income wherein it stated "Even if the decision in Warren were applicable to the present case we would decline to follow it." (Appendix D, *infra* p. 20a).

3. The decision of the Court of Appeals for the Federal Circuit is also in conflict with that part of the holding in the *Warren* case which expressly held that "The estate tax charitable deduction should be computed on the basis of what the charities will receive under Article V of the will pursuant to the probate court's judgment." In this connection, the record in this case shows that the charitable deduction claimed on the estate's federal estate tax return (Form 706) amounted to the sum of $8,869,080.10, and that the charity actually received distributions from the personal representative of the estate greatly in excess of the amount claimed, totalling $10,091,707.94. Therefore assets of the decedent's residuary estate have passed to the charity in an amount not less than $8,869,080.10, the amount of the charitable deduction claimed, as authorized by § 2055 of the Code, and that the decision in the instant case is in irreconcilable conflict on this point, with that of the Fifth Circuit in the *Warren* case.

4. The petitioner therefore respectfully suggests to the Court that the decision of the United States Court of Appeals for the Federal Circuit is therefore in conflict with the two very important points covered by the Fifth Circuit in the *Warren* case, namely:

(a) that administrative expenses paid by an estate from post-mortem income do not reduce the amount of the estate's corpus passing to charities where a residuary bequest is made, and that § 2055 allows the deduction for charitable purposes undiminished by the payment of the administrative expenses in this context; and

(b) that the charitable deduction under § 2055 should be computed and based upon the actual amounts received by the charity pursuant to the terms of the decedent's Will and any relevant probate court orders that may have been issued, during the course of the administration of the decedent's estate.

On both scores the decision in the instant case is in conflict with that of the Fifth Circuit in the *Warren* case. We urge the Court to grant this petition in order to resolve these obvious conflicts between the circuits.

If the Court permits this decision to stand then taxpayers within the jurisdiction of the United States Court of Appeals for the Fifth Circuit in the States of Texas and Louisiana will receive entirely different tax treatment than those who are subject to the jurisdiction of the United States Court of Appeals for the Federal Circuit and the United States Claims Court, in cases involving the identical issue.

5. The decision of the Court of Appeals is also in conflict with several other decisions which have held that the amount of the charitable deduction for federal estate tax purposes under § 2055 and predecessor sections of the Code should be computed on the basis of what the charities actually receive under the terms of the decedent's Will and any state statutes or probate court orders as follows:

(a) The decision of this Court in *Harrison v. Northern Trust Co., et al.*, 317 U.S. 476 (1943), wherein the Court stated in a

similar estate tax charitable deduction case that ". . . the amount to be deducted from decedent's gross estate on account of the bequest of his residuary estate to charity is the actual amount of such bequest, after payment of federal estate taxes, or what would have been the amount if there been no such taxes." In the instant case the actual amount of the residuary estate passing to the Foundation was equal to and not less than the exact amount claimed as a charitable deduction on the return of $8,869,080.10, since the controversial administrative expenses were not paid from the corpus of the decedent's residuary estate, but instead were paid from the accumulated post-mortem income realized from the administration of the estate.

(i) The United States Court of Appeals for the Eighth Circuit in *Estate of Edward H. Luehrmann v. Commissioner,* 287 F.2d 10 (8th Cir. 1961) in commenting on the Court's decision in *Harrison v. Northern Trust Co., et al.* stated "While Northern Trust dealt with the deduction of inheritance taxes in determining the value of the charitable bequest, we believe that it does clearly indicate a view on the part of the Court that the charitable deduction allowed by § 812(d) shall not exceed the amount of the residue passing to the charitable beneficiaries."

The petitioners in *Luehrmann* had argued that *Northern Trust* dealt only with the deduction of estate taxes and that since the deduction involved in their case pertains to administrative expenses rather than estate taxes that their factual situation did not fall within the coverage of the amendment. The court in *Luehrmann* stated further "A number of courts have taken the position that in instances where a charity compromises or settles an adverse claim to the charitable devise or bequest, only the amount actually received by the charity is available as a charitable deduction." Citing the decision in *Heim v. Nee*, 40 F. Supp. 594, 595 (W.D. Mo. 1937), wherein Judge Otis states: "The amount to be deducted for testamentary charitable gifts must be computed on

the basis of what the charities actually receive, not on the basis of what is provided in the will of the decedent." As repeatedly set forth in this petition, the charitable foundation received assets from the decedent's estate in excess of the amount claimed as a charitable deduction on the estate's estate tax return, and therefore under the authority of *Northern Trust* and related decisions, the deduction should be allowed as claimed.

(b) The decision in this case is also in conflict with the *Estate of Harry E. Wright, Jr. v. United States,* 677 F.2d 53 (9th Cir. 1982) which held in an estate tax charitable deduction case that "The paramount concern, for federal tax purposes, is with the real distribution of the funds rather than their nominal source" and the court continued "[t]he amount to be deducted for charitable gifts must be computed on the basis of what the charities actually received, not on the basis of what is provided in the will" citing *In Re: Sage's Estate,* 122 F.2d 480, 484 (3rd Cir. 1941).

(c) The decision in this case is also in conflict with a decision of the United States Court of Appeals for the Eighth Circuit in *William J. Oetting, Exec. v. United States,* 712 F.2d 358 (8th Cir. 1983) which held that in an estate tax charitable deduction case arising under § 2055 of the Code "A deduction is claimed only for those amounts that were actually received by the four charities. The deduction should be allowed." Here again, the Eighth Circuit is emphasizing that the amount allowable as a charitable deduction under § 2055 is to be computed on the amount that the charity or charities actually received. In this case the charitable foundation actually received principal from the decedent's residuary estate having a market value and an amount not less than the amount claimed as a charitable deduction on the federal estate tax return, in the amount of $8,869,080.10.

6. The issue in this case has also arisen in the marital deduction area of federal estate taxes, provided by § 2056 of the Internal

Revenue Code. Frequently the cases arise under substantially identical circumstances to the instant case, in situations where residual marital bequests are made and administrative expenses, instead of being paid from the principal of the estate, are paid from post-mortem income accumulations. The issue raised is identical as to whether or not the claimed marital deduction must be reduced by the amount of the administrative expenses or whether it should be allowed undiminished by the payment of administrative expenses, from accumulated post-mortem income.

Two recent decisions of the Tax Court involving this question in the marital deduction field are in the *Estate of Walter E. Richardson v. Commissioner,* 89 T.C. 1193 (1987) and in the *Estate of Gordon P. Street v. Commissioner,* T.C. Memo 1988-553, 56 TCM 774 (1988).

The Tax Court in *Richardson* held that certain estimated interest payments on federal estate taxes and state inheritance taxes, and on deficiencies with regard to said taxes is chargeable to the *income* of the estate, and did *not* reduce the amount of the marital deduction to the estate allowable under § 2056(a) of the Code.

The Tax Court in this connection stated in part:

> The principal issue remaining for decision is whether interest payable by petitioners on federal estate taxes and State inheritance taxes and on deficiencies with regard to such taxes, is chargeable against the principal of the estate or the income produced by the principal. *If the interest is chargeable against income, it will not reduce the value of the interest in the estate that will pass to the surviving spouse under the Will and consequently will not reduce the amount of the marital deduction.*

In the *Street* case, the Tax Court, speaking through Judge Tannewald, held that the expenses of administration and interest payable on State inheritance and federal estate taxes were payable from the income of the estate, and thus did not reduce the amount of the principal eligible for the estate tax marital deduction.

The Tax Court, in part, stated:

> The primary issue for decision is whether administrative expenses and interest payable on State inheritance taxes, federal estate taxes, and deficiencies related thereto, are chargeable to the principal of the estate or to the income generated therefrom. If they are chargeable to the income, they do not reduce the amount of the principal passing to the surviving spouse, and hence qualify for the marital deduction.

Unfortunately, from the taxpayer's standpoint, the decision of the Tax Court in *Street* was partially reversed and partially affirmed by the decision of the Sixth Circuit, 974 F.2d 723 (6th Cir. 1992).

We call these Tax Court decisions to the attention of the Court for the sole purpose of showing the frequency with which the question involved in this case arises and also the fact that the issue not only involves the computation of the charitable deduction for federal estate taxes under § 2055, but also the marital deduction prescribed by § 2056(a).

7. We urge the Court to grant this writ, even though the issue involved in this case is not of earth-shaking consequences. The issue, however, has been repeatedly raised before the lower federal courts for many years, and currently rises primarily in the area involving determining the amount of a charitable deduction

allowable for federal estate tax purposes and the amount of the allowable marital deduction for federal estate tax purposes. These courts include the United States Tax Court, U.S. District Courts, Court of Claims and various Courts of Appeal, and we think the conflict between the circuits on this issue should be resolved by a definitive decision of this Honorable Court.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that this petition for writ of certiorari should be granted.

Respectfully submitted,

WILLIAM R. FRAZIER
Counsel of Record
FRAZIER & FRAZIER
Attorneys for Petitioner
1515 Riverside Avenue, Suite A
Jacksonville, Florida 32204
(904) 353-5616

APPENDIX A — JUDGMENT OF THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT DATED JUNE 2, 1993

UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

92-5062

JAMES W. BURKE, as Personal Representative of the ESTATE OF EDNA SPROULL WILLIAMS, deceased,

Plaintiff-Appellant,

v.

THE UNITED STATES,

Defendant-Appellee.

JUDGMENT

ON APPEAL from the UNITED STATES COURT OF FEDERAL CLAIMS

in CASE NO(S). 540-89T

This CAUSE having been heard and considered, it is

ORDERED and ADJUDGED:

AFFIRMED

DATED JUN 02 1993

Appendix A

ENTERED BY ORDER OF THE COURT
s/ Francis X. Gindhart
Francis X. Gindhart, Clerk

ISSUED AS A MANDATE: June 23, 1993

APPENDIX B — OPINION OF THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT DATED JUNE 2, 1993

92-5062

JAMES W. BURKE, as Personal Representative of the ESTATE OF EDNA SPROULL WILLIAMS, Deceased,

Plaintiff-Appellant,

v.

THE UNITED STATES,

Defendant-Appellee.

DECIDED: June 2, 1993

Before NIES, *Chief Judge,* PLAGER and RADER, *Circuit Judges.* NIES, *Chief Judge.*

James W. Burke, as personal representative of the estate of Edna Sproull Williams, appeals from the summary judgment entered by the United States Court of Federal Claims[1] in *Burke v. United States,* No. 540-89T (Cl. Ct. Nov. 27, 1991), that Williams' estate is not entitled to a refund for taxes paid based on the federal estate tax return filed November 24, 1982.

---

1. Congress changed the name of the United States Claims Court to the United States Court of Federal Claims, effective October 29, 1992. Pub. L. No. 102-572, § 902(a), 106 Stat. 4506, 4516 (1992).

Appendix B

I.

Edna Sproull Williams died testate on February 28, 1982, while a resident of Jacksonville, Duval County, Florida. James W. Burke is the presently acting personal representative of the Williams estate. Williams' will was filed for probate in the Circuit Court for Duval County, Florida (the probate court) on March 2, 1982.

On November 11, 1982, Burke petitioned the Florida probate court to construe Articles I and XIII of Williams's will under Florida law[2] as authorizing payment of administrative expenses out of the income earned by the estate over the probate period (post-mortem income), rather than requiring payment out of the principal of the estate. Articles I and XIII of Williams' will provide:

> *Article I*
>
> I direct that all my just debts, including expenses of my last illness and funeral expenses be paid by my Personal Representatives as soon as reasonably

2. Florida statute states:

> Unless the will otherwise provides . . . all expenses incurred in connection with the settlement of a decedent's estate, including debts, funeral expenses, estate and other death taxes, family allowances, fees of attorneys and personal representatives, and court costs shall be charged against the principal of the estate.

Fla. Stat. Ann. § 738.05(1) (West Supp. 1992).

convenient after my death. I direct that all estate, inheritance and succession taxes that may be levied against my estate, including such taxes levied against property constituting any part of my estate for federal estate tax purposes, whether passing under this Will or otherwise, shall be paid by my Personal Representatives solely out of the residuary estate being bequeathed hereunder, it being my intention that the portion of my estate devised and bequeathed to or for the benefit of all legatees hereunder, except the residuary legatee, shall be enjoyed by them free from any burden for such estate, inheritance or succesSlon taxes. . . .

Article XIII

I give, devise and bequeath all of the rest, residue and remainder of my estate, including all lapsed legacies or devises, after paying therefrom any debts and taxes, including estate, inheritance, or succession taxes and other obligations of my estate, including all administration expenses, to the Trustees of the Edna Sproull Williams Foundation. . . .[3]

On November 12, 1982, only one day after the unopposed petition for construction was filed, the Florida probate court entered an Order construing the will as follows:

---

3. The Edna Sproull Williams Foundation (hereinafter the "Foundation") qualifies as a charity for purposes of federal estate taxation.

Appendix B

> Articles I and XIII of the decedent's Will are construed to authorize payment of the administrative expenses by the Personal Representatives out of income if they choose to pay such expenses out of income, and to the extent that the Personal Representatives do not choose to pay administrative expenses out of income, such administrative expenses shall be paid out of the residuary share of the estate prior to distribution to the residual beneficiary, as requested in the Petition.

Burke filed the estate's federal estate tax return on November 24, 1982. On the tax return, the entire gross estate was valued at $10,489,753.94. However, the estate claimed deductions totaling $9,747,444.42, leaving a taxable estate of $742,309.52. Included within the total claimed deductions, were charitable deductions totalling $9,662,605.10, of which $8,869,080.10 represented the will's residual bequest to the Foundation. Burke also filed a fiduciary estate income tax return covering income earned by the estate after Williams' death in 1982. On the estate's fiduciary income tax return for 1982, Burke claimed a deduction of $144,441.00 for administrative expenses incurred in administering the estate. With this income tax return, Burke also filed an elective statement under I.R.C. section 642(g) in which the estate waived its right to deduct administrative expenses on the estate's estate tax return.

After auditing the estate tax return, the Commissioner determined that the administrative expenses claimed as a deduction on the estate's income tax return should have been shown on the estate's estate tax return as reducing the charitable deduction which was based upon the residuary clause's bequest to

the Foundation. The Commissioner, thus, reduced the amount of the charitable deduction claimed by the estate by $236,536.38 — the amount of the administrative expenses plus the estate taxes attributable thereto — and assessed an estate tax deficiency of $80,110.87 against Williams' estate. The estate paid the deficiency and brought suit in the Court of Federal Claims, seeking a refund of $110,717 (the $80,110.87 deficiency plus interest).

In response to both parties' cross-motions for summary judgment, the Court of Federal Claims began its analysis by noting that, under the Florida statute, administrative expenses must be paid out of the principal estate unless the will provides otherwise, i.e., unless the will states that such expenses may be paid out of post-mortem income. Further, noting that it was not bound by the Florida probate court's interpretation of the will, the Court of Federal Claims held that "the will did, in fact, provide for the payment of administrative expenses out of the preresidue principal" in Article XIII. *Burke,* No. 540-89T, slip op. at 5-6. The Court of Federal Claims, thus, concluded that the administrative expenses of Williams' estate were required to be paid out of the principal estate.

Before the Court of Federal Claims, Burke argued that the charitable deduction attributable to the residuary bequest to the Foundation should not be decreased because, regardless of the Florida statutory requirement, the administrative expenses had in fact been paid out of post-mortem income and the Foundation had accordingly received a donation at least equal to the amount of the residuary. In response, the court held that "post-mortem income cannot be used to increase the amount of a charitable residual legacy, even by indirectly increasing the amount in the residual bequest." *Id.* at 7. Accordingly, the Court of Federal Claims granted the government's motion for summary judgment. It is from this summary judgment that Burke appeals.

Appendix B

II.

On appeal, Burke does not assert that the Court of Federal Claims erred by granting summary judgment over the existence of a genuine issue of material fact. Rather, Burke argues only that the trial court erred as a matter of law. Burke first argues that the Court of Federal Claims erred as a matter of law by construing Williams' will under Florida law as not allowing payment of the estate's administrative expenses out of post-mortem income, particularly in light of the Florida probate court's decision allowing such payment. Burke also argues that the estate's residuary charitable deduction should not be reduced by the amount of the administrative expenses as a matter of law because the estate in fact[4] paid the administrative expenses out of post-mortem income. The Commissioner argues, not surprisingly, that the Court of Federal Claims correctly interpreted the will and that the use of post-mortem income to pay administrative expenses does not alter the result that the residuary charitable bequest must be reduced by the amount of the administrative expenses for federal estate tax purposes.

While we do not find error in the Court of Federal Claims' determination that under Florida law the will required administrative expenses to be paid out of the principal of the estate,[5] we believe that the emphasis on the source of payment

4. Whether or not Burke actually paid the estate's administrative costs out of post-mortem income is not a genuine issue of material fact in light of our discussion below. For the purpose of our analysis, we must assume that Burke did in fact use post-mortem income to pay the administrative expenses.

5. Addressing the effect of a state court probate determination where the matter decided is determinative of federal estate tax consequences, the Supreme Court has

(Cont'd)

allowable under state law shifts the focus of the case from the pertinent question — whether payment of administrative expenses must be accounted for in computing the value of a taxable estate under federal law for federal estate tax purposes regardless of the actual source of payment.

A.

We have no quarrel with Burke's interpretation of the Florida statute as allowing a decedent to provide for the payment of administrative expenses out of post-mortem income. The Florida statute reflects the reality that often times it may be in the best interest of an estate to pay administrative expenses from post-mortem income instead of from principal. This payment method avoids forcing the personal representative to sell off portions of an estate to cover expenses. For example, emergency sales of personal property such as stocks or real property could unnecessarily deplete the value of the estate.

Nonetheless, while state law may allow for various sources of payment for administrative expenses, such allowance does not necessarily affect the treatment of these expenses for federal estate taxation purposes. As our predecessor court has stated, "Generally speaking, state law is determinative of property rights, while the manner and extent to which such rights are taxed are determined by federal law." *Murray v. United States,* 687 F.2d 386, 392 n.3 (Ct. Cl. 1982) (citing *Morgan v. Commissioner,* 309 U.S. 78, 80-81 (1940)). In other words, the allowable sources of *payment* for

---

(Cont'd)
stated, "[W]hen the application of a federal statute is involved, the decision of a state trial court as to an underlying issue of state law should *a fortiori* not be controlling." *Commissioner v. Estate of Bosch,* 387 U.S. 456, 465 (1967).

administrative expenses under *state* law does not necessarily affect the source from which the *deduction* for administrative expenses must be made under *federal* law. *See Lyeth v. Hoey, Collector of the Internal Revenue,* 305 U.S. 188, 193-94 (1938). Therefore, we must examine the federal estate tax statutes in order to determine if payment of administrative expenses from post-mortem income, as potentially allowed by state law, somehow affects a residuary charitable bequest.

B.

Section 2001 of the Internal Revenue Code imposes a tax on the transfer of the "taxable estate" of every decedent who is a citizen or resident of the United States. I.R.C. § 2001.[6] To evaluate a decedent's taxable estate for purposes of section 2001, the administrator must first ascertain the value of the decedent's "gross estate." This value is defined by statute as "the value *at the time of death* of all property, real or personal, tangible or intangible, wherever situated." I.R.C. § 2031(a) (emphasis added).[7] The taxable estate is then calculated by subtracting any amounts qualifying as deductions under sections 2053-2056 from the value of the decedent's gross estate. I.R.C. § 2051. With respect to this case, the deductions at issue are those provided in section 2053 for administrative expenses and in section 2055 for charitable donations.

Section 2051 allows the deduction of various amounts "from

---

6. Unless otherwise specified, the statutes and regulations cited hereinbelow are those covering 1982.

7. Section 2032 provides an alternative valuation scheme which does not apply in this case.

the value of the gross estate" in order to determine the taxable estate. One of these deductible amounts is provided for in section 2053 which states that "the value of the taxable estate shall be determined by deducting from the value of the gross estate [administrative expenses] as are allowable by the laws of the jurisdiction . . . under which the estate is being administered." Although section 2053 permits state law to determine what administrative expenses are "allowable," how section 2053 treats the allowable administrative expenses for estate tax deduction purposes is a federal question. *See Lyeth,* 305 U.S. at 193-94.

Section 2051 defines the taxable estate and the deductions used to determine the taxable estate in terms of the gross estate. *See* Treas. Reg. § 20.2051-1 (taxable estate determined by subtracting total amount of deductions "from the total amount which must be included in the gross estate"). Likewise, section 2053, by its plain language, defines the deduction for administrative expenses in terms of the gross estate. Reading sections 2031, 2051, and 2053 together, the gross estate, which is the value of the decedent's estate at the time of death, is the sole source from which the administrative expenses may be deducted.[8] Thus, the deduction of administrative expenses as provided for by federal law — as opposed to the actual payment of administrative expenses as allowed under state law — must come from, i.e., be accounted for within, the gross estate. *See Estate of Street v. Commissioner,* 974 F.2d 723, 728-29 (6th Cir. 1992); *Alston v. United States,* 349 F.2d 87, 88 (5th Cir. 1965); *Estate of Horne v.*

---

8. While the tax code apparently allows an estate to elect to *claim* a deduction for administrative expenses on the estate's income tax return instead of on the estate's estate tax return, after filing a waiver under section 642(g), both parties have stipulated that section 642(g) is wholly immaterial to the determination of the charitable deduction to which the present estate is entitled.

Commissioner, 91 T.C. 100 (1988). In other words, regardless of the source of payments for administrative expenses, such payments are charges against the gross estate and must be accounted for accordingly. *See Estate of Street,* 974 F.2d at 728-29 (if estate income is used to pay administrative expenses so as to increase the residue passing to the surviving spouse, the value of the additional residue cannot be included in the amount for the marital deduction); *Alston,* 349 F.2d at 88 ("Administrative expenses must be deducted from the gross estate even though paid out of post-mortem income."); *Rifkind v. United States,* 5 Cl. Ct. 362, 374 (1984) ("Insofar as the New York probate court allows an expense of administration to be paid out of post-mortem income, the accounting practice is at fatal variance with the entrenched principle of federal estate tax law that a decedent's estate must be valued at date of death . . . for purposes of deducting later incurred administration expenses.").

In sum, when a decedent dies, a finite amount known as the gross estate is legally created. Any deductions for expenses incurred in administering the estate are theoretically derived from this amount and, regardless of the actual source of payment, must be accounted for within the gross estate. *See Alston,* 349 F.2d at 88-89; *Rifkind,* 5 Cl. Ct. at 374. *See also Beckwith,* 261-3d *Tax Management Portfolio: Estate and Gift Tax Charitable Deductions* (BNA), at A-23 - A-24; 4 J. Rabkin & M. Johnson, *Federal Income Gift and Estate Taxation,* § 59.07, at 5985 (1992).

Burke argues that the only relevant provision of the tax code is section 2055 which allows a deduction from the decedent's gross estate of amounts given to a qualifying charity. Per Burke, for purposes of the section 2055 deduction, the only requirement is that the charity actually receive the amount claimed as the deduction. Burke argues that since the Foundation received more

than the amount claimed as a deduction under section 2055 over the probate period, the requirements for claiming a deduction are satisfied.

However, the fact that the charitable deduction taken on Burke's federal estate tax return was less than the actual amount received by the charity over the seven-year probate period is not determinative. The relevant inquiry is the amount received by the charity *under the will,* i.e., the amount of the gross estate that passed to the charity. That the charitable donation was augmented by post-mortem income, resulting in an overall charitable donation of an amount greater than the estate tax deduction claimed, does not increase the amount of the charitable bequest under the will.[9]

Under Williams' will, the Foundation received the residue of the estate. Therefore, the value of the gross estate that passed to the Foundation for which the estate may claim a charitable deduction under section 2055, is the amount remaining in the estate after Burke had accounted for all of the obligations of the estate accruing at the time of death. These obligations included payment of the administrative expenses for which the estate claimed a deduction, albeit on the estate's income tax return. In calculating the residue, the amount of the gross estate passing to charity under the will, Burke failed to take into account the reduction

---

9. In discussing the amount of residue of an estate qualifying for the marital deduction under section 2056, the Senate Report provides that "[i]f the decedent leaves the residue of his estate to the surviving spouse and she pays, or if estate income is used to pay, claims against the estate so as to increase the residue, such increase in the residue is acquired by purchase and not bequest. Accordingly, the value of any additional part of the residue passing to the surviving spouse cannot be included in the amount for the marital deduction." S. Rep. No. 1013, 80th Cong., 2d Sess. II-6 (1948). While the above provision is framed in the context of the marital deduction, the logic is no less applicable to the present case.

necessitated by administrative expenses. This was error because, for purposes of federal estate taxation, the gross estate is obligated to pay those expenses. In essence, Burke would have us indirectly increase the value of the gross estate by allowing him to use post-mortem income to pay the obligations of the gross estate. While, as we have previously noted, it may be beneficial or convenient to pay such obligations out of post-mortem income, the post-mortem income so used does not itself become part of the gross estate. The result Burke seeks would allow the estate to claim two deductions for the exact same portion of the gross estate as being both an administrative expense deductible under section 2053, which Burke elected to claim on the estate's income tax return, and a charitable donation deductible under section 2055, which Burke claimed on the estate tax return.

The amount of the charitable deduction claimed by Williams' estate was properly reduced by the amount of administrative expenses claimed as a deduction on the estate's fiduciary income tax return because, for federal estate taxation purposes, only this lesser amount was paid to the charity *from the gross estate.* The additional amount paid to charity over the probation period was post-mortem income for which estate received a deduction on its federal income tax returns.

During the pendency of this case, Burke submitted a recent decision, *Estate of Warren v. Commissioner,* No. 91-4401 (5th Cir. Jan. 13, 1993), which he offers in support of his contention that administrative expenses may be paid from post-mortem income without diminishing the amount of the residue passing to charity. Other than the law as determined by the United States Supreme Court, we are bound only by the decisions of the United States Court of Claims and the United States Court of Customs and Patent Appeals, *see South Corp. v. United States,* 690 F.2d 1368, 1370

(Fed. Cir. 1982) (in banc). Thus, we need only consider the Fifth Circuit's decision in *Warren* for its persuasiveness. For the reasons stated in the discussion below, *Warren* does not alter the outcome of this case.

In *Warren,* the decedent's will established two residuary charitable trusts which were to pay annuities to the charities each year equal to eight and one-half percent of the initial fair market value of the trust assets. After twenty years, the trust assets were to be divided among Warren's children and grandchildren. The potential for dispute becomes readily apparent — the higher the payment to the charities throughout the life of the trust, the lower the value of the trust assets which will subsequently be divided among the children and grandchildren. The decedent's estate incurred substantial administrative costs, which, if paid in total from the residuary, would have established relatively small annuity payments for charities and relatively large trust assets at the end of twenty years to be divided among the children and grandchildren.

The charities brought suit in the probate court claiming that the estate's administrative expenses should be paid out of post-mortem income in order to preserve the principal of the trust. The parties settled the case and the probate court entered an agreed final judgment. The parties' agreement provided that 27 1/2 percent of the administrative expenses would be charged to the estate's corpus and 72 1/2 percent of the administrative expenses would be charged to residuary post-mortem income.[10]

---

10. These percentages were apparently based on a Texas trust statute which allocates 27 1/2 percent of the income earned by trusts comprising oil and gas assets to the principal of the trust and 72 1/2 percent to income earned by the trust. Texas Trust Code, Tex. Prop. Code Ann. § 113.107(d) (West 1984).

Appendix B

After auditing the estate's estate tax return, the Commissioner asserted an estate tax deficiency. Before the Tax Court, the Commissioner argued that the estate had improperly failed to decrease its charitable donation deduction by the full value of the administrative expenses. The estate argued that, according to the agreed settlement judgment entered by the probate court, the charitable donation claimed on the estate tax return had to be reduced only by 27 1/2 percent of the administrative expenses. The Tax Court determined that it was not bound by the probate court's judgment and agreed with the Commissioner.

On appeal, the Fifth Circuit concluded that the *Bosch* rule, that a state trial court probate decision does not control the application of the federal estate tax statute,[11] was limited to situations in which the state court's decision was the result of non-adversarial proceedings. Therefore, per the Fifth Circuit, the Tax Court was bound by the state probate court's decision because it resulted from a bona fide adversarial proceeding between the various beneficiaries under the will. The Fifth Circuit also found it significant that the government failed to submit evidence supporting its allegation that the settlement between the parties was structured to avoid federal tax liability.

In the case at bar, there was no *bona fide* adversarial proceeding leading to the Florida probate court's decision to allow payment of administrative expenses out of post-mortem income. Therefore, even assuming that *Bosch* is limited to non-adversarial situations, it is applicable to this case. Moreover, neither of the parties in this case contends that the Court of Federal Claims or the Federal Circuit should be bound, as opposed to merely influenced by the Florida probate court's decision.

---

11. *See supra* note 5.

Appendix B

Even if the decision in *Warren* were applicable to the present case we would decline to follow it. By allowing state court decisions to bind federal courts on issues which are clearly federal tax law issues, *Warren* would subject the federal tax system to "the whim of the state courts or legislatures." *Estate of Street,* 974 F.2d at 728. Further, the decision in *Warren* would allow an agreement between the beneficiaries under a will to dictate federal estate tax law. While the settlement in *Warren* was undoubtedly the result of adversarial proceedings, it is hard to imagine that reducing federal estate tax consequences was not at least one aspect of the settlement agreement. Decreasing the amount of taxes owed would increase the overall post-tax amount of money which could be divided by both of the negotiating parties. Moreover, the Fifth Circuit's holding in *Warren* appears contra to its earlier decision in *Alston v. United States, supra,* in which the court held that "administrative expenses must be deducted from the gross estate even though paid out of post-mortem income." *Alston,* 349 F.2d at 88.

CONCLUSION

The Court of Federal Claims correctly held that, as a matter of federal law, Burke could not indirectly increase the amount of the charitable residual legacy by paying administrative expenses out of post-mortem income. Accordingly, we affirm the trial court's decision that the Commissioner correctly reduced the estate's claimed charitable deduction to account for the amount of the administrative expenses deducted from the estate's income taxes and that Williams' estate is not entitled to a refund.

AFFIRMED

APPENDIX C — OPINION OF THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT DATED JUNE 2, 1993

OPINION ANNOUNCING
JUDGMENT OF THE COURT

OPINION FILED AND JUDGMENT ENTERED: JUN 02 1993

The attached opinion announcing the judgment of the court in your case was filed today. The judgment was also entered pursuant to Rule 36. The mandate will be issued in due course.

Costs may be recoverable under Rule 39 or as the court may have directed in the opinion. A party entitled to costs is provided with a bill-of-costs form and an instruction sheet with this notice.

The parties are encouraged to stipulate to the costs. A bill of costs will be presumed correct in the absence of a timely filed objection.

Costs when taxed are payable to the party awarded its costs. If costs are awarded to the government, they should be paid to the Treasurer of the United States. Payment should be made to counsel for the party awarded costs or, if the party is not represented by counsel, to the party pro se. Costs should be paid promptly.

If the court also imposed monetary sanctions, they are payable to the opposing party unless the court's opinion provides otherwise. Sanctions should be paid in the same way as costs.

Exhibits and visual aids shall be promptly retrieved by the party that lodged them with this court.

Appendix C

FRANCIS X. GINDHART
Clerk

BURKE V US, 92-5062
(CLM - 540-89T)

[stamped]
RECEIVED
JUN 07 1993

APPENDIX D — DECISION OF THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT IN THE CASE OF ESTATE OF DOROTHY J. WARREN, DECEASED, ET AL. V. COMMISSIONER OF INTERNAL REVENUE DATED JANUARY 13, 1993

[¶ 60,127] Estate of Dorothy J. Warren, Deceased, River Oaks Trust Company and R. Clay Underwood, Co-Administrators with Will Annexed of the Estate of Dorothy J. Warren, Deceased, Petitioners-Appellants v. Commissioner of Internal Revenue, Respondent-Appellee.

U.S. Court of Appeals for the Fifth Circuit, No. 91-4401, January 13, 1993. Reversing and remanding the decision of the United States Tax Court, 60 TCM 206, CCH Dec. 46,742(M).

[Code Sec. 2055]

Estate tax: Deductions: Charitable transfers: Allocation of administration expenses. — An estate was entitled to allocate 27 1/2 percent of its administrative expenses against residuary assets passing to charitable lead trusts and 72 1/2 percent of the expenses to the estate's postmortem income pursuant to a state (Texas) probate court decree. Although the decedent's will provided that all administration expenses were to be paid from the residuary estate, the state court decree modified and approved a settlement that resolved adversarial, nontax, bona fide disputes between the parties. Concluding that the state court decree was valid and binding under Texas law, the court followed the approach in Rev. Rul. 89-31, 1989-1 CB 277, rather then *H. J. Bosch Est.*, 67-2 USTC ¶ 12,472, 387 US 456, holding that the estate tax charitable deduction must be computed on the basis of what the charities received under the will pursuant to the state court decree. Back reference: ¶ 7425.18.

Appendix D

Before *Reynaldo G. Garza, Garwood,* and *Duhé*, Circuit Judges.

Garwood, Circuit Judge: Petitioners-appellants, the estate of Dorothy J. Warren and its administrators (together, the Estate) appeal the judgment of the United States Tax Court essentially upholding the Internal Revenue Service's estate tax deficiency determination against the Estate. We reverse.

I

Facts and Proceedings Below

The deceased, Dorothy J. Warren (Warren), a Texas resident, was a wealthy divorcee with several children and grandchildren, and an affinity for two Catholic charities in Houston (the Charities). When she died on May 27, 1983, she left a will, executed in 1981, disposing of her estate, which at the time of her death had a gross value of approximately $28 million. Most of the estate's assets consisted of oil and gas leases, or interests therein, in Texas and Louisiana. Article V of the will put the bulk of the estate into two equal residuary trusts, the Charitable Lead Children's Trust and the Charitable Lead Grandchildren's Trust (the Trusts). The Trusts provided for a fixed annual annuity payment to the Charities for twenty years. The annuity amount was specified as "an amount equal to eight and one-half percent (8 1/2%) of the initial net fair market value of the assets constituting the trust." The annuity amount was to be paid every year from trust income. If excess income were generated in a year, such excess was to be added to the trust corpus. If the income was not sufficient to pay the annuity amount, however, the balance would be paid out of the trust corpus.

At the end of twenty years, the remaining trust assets were to be distributed to the children and grandchildren. This arrangement

was instituted primarily to further Warren's testamentary goals in a way that minimized that tax burden on the estate. The large guaranteed annuities to the Charities assured that much of the estate would qualify for the charitable bequest deduction of Internal Revenue Code (Code) § 2055(a) & (e)(2)(B), 26 U.S.C. § 2055(a) & (e)(2)(B) (West 1989).

Warren's will was admitted to probate in September 1983 in Probate Court No. 3 of Dallas County, Texas (the Probate Court). Between 1983 and 1987 approximately sixteen separate law suits were filed by or against the estate in the Probate Court, including suits by creditors and suits challenging the construction and administration of the will and estate. These suits involved, among others, all the beneficiaries and legatees of the will and dragged on for several years.

Because of the reorganization of several of the business enterprises that comprised a substantial part of Warren's assets, the administrative expenses incurred throughout the long course of probate proceedings swelled to over $8.5 million by July 1988 and over $9 million by November 1989. Approximately $2 million of these expenses were paid from Estate principal. Due to the extended time involved, the Estate also realized substantial postmortem income from the Estate's assets.[1] Article III of Warren's will provided that:

> "All of my just debts, funeral expense, administration and testamentary expenses, and all estate, inheritance, transfer, and succession

---

1. By "postmortem income" we mean income derived from estate assets between the time of Warren's death and the time the probate of her estate was substantially completed.

> taxes . . . shall be paid out of my residuary estate passing under Article V hereof, without apportionment."

Article V of the will states that " 'my residuary estate' " is to "consist of my entire testamentary estate after satisfaction of any gifts under Article IV hereof, and after payment of those debts, expenses, and taxes referred to in Article III hereof."

Because the huge administrative expenses, if deducted from the residuary corpus, would have substantially reduced the annuity amount, the Charities brought suit in the Probate Court claiming, *inter alia,* that these expenses should be paid out of residuary postmortem income rather than the residuary corpus.[2] The parties found ambiguity in the will's use of the terms "residuary estate" and "initial net fair market value" and argued extensively about whether the administrative expenses should be charged to the residuary corpus or postmortem income.

---

2. This postmortem income consisted largely of income from oil and gas holdings of a kind that the provisions of the Texas Trust Code, Tex. Prop. Code Ann. § 113.107(d) (West 1984) (formerly Vernon's Ann. Tex. Civ. Stat. art. 7425b-33), direct that trusts apportion 27 1/2 % (but not to exceed 50% of the net after deducting the property's expense and carrying cost) to trust corpus and the balance to income. The Texas Trust Code also provides that "[i]f an asset becomes subject to a trust under a will, it becomes subject to the trust as of the date of the death of the testator, even though there is an intervening period of administration of the testator's estate," Tex. Prop. Code § 113.103(a) (formerly Vernon's Ann. Civ. Stat. art. 7425b-28) and that "[i]f the provisions of . . . [the Texas Trust code] and the terms of a trust conflict, the terms of the trust control." *Id.* § 111.002(a). Article II of the Will granted the estate's personal representative, among other things, "all of the rights and powers conferred upon a trustee by the Texas Trust Act and other laws of Texas." Texas Property Code Ann. § 113.019 (West 1984) (formerly Vernon's Ann. Tex. Civ. Stat. art. 7425b-25) grants trustees the power to compromise and settle claims.

Appendix D

The parties to most of the suits, including the administrators, the Charities, the children and grandchildren, and most claimants against the Estate, were finally able to reach a settlement of their claims in July 1987. Included in this omnibus settlement was a provision that Article III of the will would be restated to allocate payment of all administrative expenses out of the residuary postmortem income, not out of the residuary corpus.

The Probate Court modified and approved the settlement and entered an agreed final judgment in September 1988. The Probate Court found that because (i) the income from the oil and gas interests would be allocated 27 1/2% to principal and 72 1/2% to income,[3] and (ii) the postmortem income was the only liquid asset available to the residuary estate to pay the administrative expenses, the administrative expenses should be allocated accordingly. Thus, the agreed final judgment provided that 27 1/2% of the administrative expenses would be charged to the residuary corpus and 72 1/2 % of the administrative expenses would be charged to residuary postmortem income.[4] It was also provided that the annuity amount would in no event be less than $1,471,575.81 per year.

Respondent-appellee, the Commissioner of Internal Revenue (the Commissioner), having asserted an estate tax deficiency, the

---

3. See note 2, *supra*.

4. The judgment provided that the will's Article V "the initial net fair market value of the assets constituting" each of the two Trusts would be one-half of the amount calculated as follows, *viz*, the total gross estate as calculated for federal estate tax purposes less the specific bequests in Article IV, less 27 1/2% of the administrative expenses paid to date, and less all of each of the following: funeral expenses, debts of decedent, mortgages and liens, and federal estate taxes and state death taxes.

Estate filed a petition for redetermination in the Tax Court. Most of the issues were settled.[5] However, there remained for trial the issue of whether in calculating the amount of the estate tax charitable deduction for the bequest to the Trusts under Article V of the will the amount of "the initial net fair market value of the assets constituting the" Trusts should be reduced by one hundred percent of the Estate's administrative expenses, as claimed by the Commissioner, or only by the 27 1/2% thereof pursuant to the Probate Court's judgment, as asserted by the Estate. The Tax Court agreed with the Commissioner, determining that it was not bound by the Probate Court's judgment and that under Texas law Warren's will required that all the administrative expenses be charged to the residuary corpus before computing "the initial net fair market value of the assets constituting the trust," eight-and-one-half percent of which was to constitute the annual annuity amount payable to the Charities over the twenty-year term. Following the

---

5. The initial estate tax return filed by the Estate in 1984 left many of the crucial items blank or "undetermined." The Commissioner issued a notice of deficiency in the amount of $34,340,734.68, which the government's brief states was "based largely on the values for the assets and debts of the estate contained in the marriage Settlement Agreement between the decedent and her fomer husband that had been executed the year before her death," although the Estate asserts that "the bulk" of the deficiency "resulted from" the Commissioner's position that the Charities "were not qualified charitable organizations." In any event, it was eventually agreed: that the value of the total gross estate for estate tax purposes was $28,352,319.92; that as of July 31, 1988, the Estate had incurred and paid $8,523,834.44 ($9,085,849.61 as of November 28, 1984) in administrative expenses and that such expenses were allowable as a deduction for estate tax purposes under Code § 2053(a)(2) to the extent the Estate elected to so deduct them (and not to deduct them for income tax purposes, see Code § 642(g)); that the Charities were qualified charities for the purposes of the estate tax charitable deduction (Code § 2055(a)); and that the Article V bequest to the Charities was in the form of a guaranteed annuity for purposes of Code § 2055(e)(2)(B).

Tax Court's opinion, final judgment was entered on the basis of an agreed "Computation For Entry of Decision." The effect of the Tax Court's decision was to reduce the amount of the annual annuity payable to the Charities, for purposes of the estate tax charitable deduction, from some $1,471,575, under the Probate Court's judgment, to $878,131, with a consequent reduction in the estate tax charitable deduction from some $16,878,827 to $10,072,070.[6] The Estate timely perfected this appeal.

DISCUSSION

In determining that it was not bound by the decision of the Texas Probate Court in allocating administrative expenses, the Tax Court relied on *C.I.R. v. Estate of Bosch* [67-2 USTC ¶ 12,472], 87 S.Ct. 1776, (1967).

In *Bosch,* and its companion case of *Second National Bank of New Haven v. United States,* the Supreme Court reviewed decisions of the Second Circuit from New York and Connecticut, respectively *C.I.R. v. Estate of Bosch* [67-2 USTC ¶ 12,491], 363 F.2d 1009 (1966), and *Second National Bank of New Haven v. United States,* 351 F.2d 489 (1965), in which the estate tax marital deduction was at issue. The New York case involved a revocable trust established by the decedent in which his surviving spouse had

---

6. The Computation For Entry of Decision calculated the estate tax charitable deduction amount as 11.4699 times the amount of the 8 1/2% annual annuity, or 97.49415%(8 1/2% x 11.4699) of the corpus of the Trusts ($10,330,948.61 after deducting from the residuary estate, *inter alia,* all the $9,085,849.61 in administrative expenses). See 26 C.F.R. §§ 20.2031-10 (Table B), 20.2055-2(e)(2)(vi), 20.2055-2(f)(2)(iv). The allowed estate tax deductions also included $3,855.05 funeral expenses, $1,656,925.75 debts, $4,809,843 mortgages and liens, and $9,085,849.61 administrative expenses (exclusive of interest). The Estate received the right, in the event the Tax Court's decision were reversed, to deduct less than all of such administrative expenses for estate tax purposes, presumably so that in that event it could instead deduct such expenses for income tax purposes. See Code § 642(g).

had a life estate with a general power of appointment as to which she subsequently, but before his death, executed an instrument purporting to release the general power and convert it into a special power. The Commissioner disallowed the marital deduction because the surviving spouse did not have a general power of appointment, due to the release instrument. While the case was pending in the Tax Court, the estate filed a proceeding in a New York trial court to declare the release of a nullity, and the New York trial court so declared it. As the Second Circuit's opinion reflects, it was conceded that the state proceeding was brought at least partially for the purpose of affecting the outcome of the Tax Court case, all concerned in the state case took the position there that the release was a nullity, and no contrary argument was presented to the state court. *Bosch,* 363 F.2d at 1011. The Tax Court and the Second Circuit, over Judge Friendly's dissent, held for the estate on the basis of the state trial court judgment, even though it was recognized that the state proceedings were essentially "non-adversary." *Id.* at 1013. The Connecticut case involved a dispute as to the amount of the marital deduction, which turned on whether the state statute apportioning estate and inheritance taxes in the absence of a contrary provision in the will applied, with a greater marital deduction resulting if the statute applied. After the Commissioner asserted a deficiency based on the inapplicability of the apportionment statute, the executor filed an application in the Connecticut Probate Court to have the estate taxes prorated under the statute, and all charged against the trust for the grandchildren rather than the marital deduction trust. Others interested in the estate, including the other beneficiaries under the will, though cited, did not contest the application, and some filed statements of no objection. The Probate Court granted the application. *Bosch,* 87 S.Ct. at 1780. The Second Circuit ultimately affirmed a summary judgment in favor of the Internal Revenue Service (IRS) on this issue, holding that the will unambiguously reflected that the state

proration statute would not apply, and that the Probate Court's contrary decision did not require a different result, noting that the judges of such courts are laymen and their decisions "are even subject to collateral attack in another probate district." *Second National Bank of New Haven*, 351 F.2d at 494.

The Supreme Court affirmed in the Connecticut case and remanded to the Second Circuit in the New York case, holding that the respective state trial court decisions were not to be given "controlling" effect. *Bosch*, 87 S.Ct. at 1782.

The Supreme Court initially noted that "at least three positions have emerged among the circuits" respecting the effect of state trial court decrees "where the matter decided there is determinative of federal estate tax consequences." *Id.* at 1781. It next described these positions without evaluating them. The first it characterized as treating the state court ruling as decisive if the issue was "fairly presented for its independent decision" and was "binding upon the parties under the state law." *Id.* The second position, characterized as "[t]he opposite view" and one which "seems to approach" the methodology employed in diversity cases to determine state law, was that the federal courts would be bound by the state court ruling "only after independent examination of the state law as determined by the highest court of the State." *Id.* The third view, advocated by the government as "an intermediate position," was that "a state trial court adjudication is binding in such cases only when the judgment is the result of an adversary proceeding in the state court." *Id.* at 1782.

The next paragraph of the Court's opinion commences by stating "[w]e look at the problem differently." *Id.* The Court explains "[f]irst" that neither *res judicata* nor *collateral estoppel* apply to the cases before it because the Commissioner was not a

party to either of the state court proceedings. It then observes that "both state proceedings were brought for the purpose of directly affecting federal estate tax liability." *Id.* "Next" the opinion points out that because the issue before it involves "a federal taxing statute," the Court "must look to the legislative history surrounding it," and then observes:

> "the report of the Senate Finance Committee recommending enactment of the marital deduction used very guarded language in referring to the very question involved here. It said that 'proper regard,' not finality, 'should be given to interpretations of the will' by state courts and then only when entered by a court 'in a bona fide adversary proceeding.' S.Rep. No. 1013, Pt. 2, 80th Cong., 2d Sess., 4. We cannot say that the authors of this directive intended that the decrees of state trial courts were to be conclusive and binding on the computation of the federal estate tax as levied by the Congress. If the Congress had intended state trial court determinations to have that effect on the federal actions, it certainly would have said so — which it did not do. On the contrary, we believe it intended the marital deduction to be strictly construed and applied. Not only did it indicate that only 'proper regard' was to be accorded state decrees but it placed specific limitations on the allowance of the deduction as set out in § 2056(b), (c), and (d)." *Id.*

The Court goes on to say that "[t]his is also in keeping

with . . . the Rules of Decision Act, 28 U.S.C. § 1652" and the Court's precedents holding that "even in diversity cases" decisions of " 'lower state courts' " though " 'attributed some weight' " are not " 'controlling' " if "the highest court of the State has not spoken on the point." *Id.* It then notes that:

> "[t]his is not a diversity case but the same principle may be applied for the same reasons, *viz.*, the underlying substantive rule involved is based on state law and the State's highest court is the best authority on its own law. If there be no decision by that court then federal authorities must apply what they find to be the state law after giving 'proper regard' to relevant rulings of other courts of the State." *Id.* at 1783.

The concluding substantive paragraph of *Bosch* states "[w]e believe that this would avoid much of the uncertainty that would result from the 'non-adversary' approach and at the same time would be fair to the taxpayer and protect the federal revenue as well." *Id.*

The precise scope and meaning of *Bosch* as applied in dissimilar contexts is difficult for us to ascertain. The Court's language "[w]e look at the problem differently" suggests that it was not entirely agreeing with any of the three general positions described, but not evaluated, in the immediately preceding paragraph of the opinion. Later language in the opinion, however, indicates that it was adopting the second position (although it never expressly so states). Was the Court, perhaps, leaving open the proper approach in other contexts, such as federal tax consequences not relating to the marital deduction, which is so

heavily emphasized as a ground for decision? We note in this connection that *Bosch* distinguished *Blair v. Commissioner,* 57 S.Ct. 330, (1937), an income tax case, on the ground that it "involved the question of a property right determination by a state appellate court." *Bosch,* at 1781 n.3. *Bosch* also involved state trial court decrees in cases brought by the taxpayer "for the purpose of directly affecting federal estate tax liability." Moreover, the opinion makes clear that adversarial positions were not taken by the parties in the state cases, not withstanding its seeming rejection of "the 'non-adversary' approach." Some authorities have concluded that *Bosch* does not vitiate the significance of *bona fide* adversarial settlements. *See Waldrup v. United States,* 499 F.Supp. 820, 824 n.4 (N.D. Miss. 1990); *but see Estate of Brandon v. C.I.R.* [87-2 USTC ¶ 13,733], 828 F.2d 493,499 (8th Cir. 1987) (marital deduction case; *Bosch* applies to good faith adversary settlements).

In the estate tax charitable deduction area, though without citing *Bosch,* controlling effect has frequently been given to *bona fide* settlements of adversarial litigation not instituted for tax purposes. *See Flanagan v. United States* [87-1 USTC ¶ 13,718], 810 F.2d 930 (10th Cir. 1987); *Estate of Strock v. United States,* 655 F.Supp. 1334 (W.D. Pa. 1987); *Northern Trust Co. v. United States,* 41 A.F.T.R.2d 78-1523 (N.D.Ill. 1977);[7] Rev. Rul. 89-31, 1989-1, C.B. 277 (revoking prior contrary ruling and holding "[i]n situations involving settlements of bona fide will contests the Service will no longer challenge the deductibility of immediate payments to charities solely on the ground that they were made in

---

7. *Northern Trust Co.* has frequently been cited with approval. *See, e.g., Oetting v. United States* [83-2 USTC ¶ 13,533], 712 F.2d 358, 361 (8th Cir. 1983); *First National Bank of Fayetteville v. United States* [84-1 USTC ¶ 13,558], 727 F.2d 741, 748 (8th Cir. 1984); Rev. Rul. 89-31, 1989-1, C.B. 277.

lieu of a split interest [provided for in the will] that would not constitute an allowable deduction under section 2055(e)(2) of the [Internal Revenue] Code"); Technical Advice Memorandum 8948004 (August 25, 1989).[8]

In *Brown v. United States,* 890 F.2d 1329, 1341-43 (5th Cir. 1989), we considered *Bosch* and ultimately concluded that "[t]he relevance of a state court's judgment to the resolution of a federal tax question will vary, depending on the particular tax statute involved as well as the nature of the state proceeding that produced the judgment." *Id.* at 1342.[9] We apply that test here and conclude

---

8. This directive applied Rev. Rul. 89-31 to a situation where the *bona fide* settlement not only gave the charity an immediate payment in lieu of the nonqualifying split interest provided for it in the will, but also provided that the charity would be exonerated from paying any portion of the estate taxes notwithstanding that the "will specifically provides that estate taxes are to be paid out of the charitable residue as an expense of administration without apportionment." In reaching this result it is stated "[a] bona fide settlement agreement results in a restructuring of the terms of the will so that the beneficiaries' interests are based on the restructured will. See Rev. Rul. 89-31, *supra.* Thus the provisions of a bona fide settlement agreement prevail over the provisions of the will."

9. In *Brown* we held the Texas Probate Court order finding that the estate, administered by an independent executor, required ongoing management and administration, did not preclude the Commissioner from determining under Treasury Regulation 1.641(b)-(3)(a) that administration of the estate had already been unduly prolonged. We noted that the executor did not file the probate proceeding until after the deficiency notice, *id.* at 1341, "the nonadversary quality" of that proceeding, and the fact that the Probate Court "was not presented with all the relevant facts and differing views." *Id.* at 1342. We further observed "[n]ot only was there no genuine controversy involved, the probate court's order was unneccessary" and "had no practical consequences apart from this federal tax controversy." *Id.* We held it was thus "entitled to little weight." *Id.*

that the Tax Court erred by not giving effect to the Probate Court judgment.

The tax statute involved here is the provision for estate tax charitable deduction, Code § 2055. In this respect, we are aware of no legislative history comparable to that cited in *Bosch* with respect to the effect of state court decrees.[10] However, as has been frequently recognized, "[i]n enacting the charitable deduction provisions in I.R.C. § 2055 and its predecessors, Congress sought to encourage gifts to charity." *Flanagan* at 934. Typically, in upholding charitable deductions based on court approved *bona fide* settlements of adversarial positions, the decisions have stressed that "[t]he deduction is sought for the actual benefit passing to the charitable foundation." *Id.* at 935. *See also Oetting v. United States* [83-2 USTC ¶ 13,533], 712 F.2d 358 at 363 (8th Cir. 1983) ("A deduction is claimed only for those amounts that were actually received by the four charities. The deduction should be allowed.").[11] That is the situation here, as the Estate seeks a deduction only on the basis of what the Charities will actually receive from the Estate. Of course, for purposes of section 2055 what is received must be received *from the decedent,* and not merely from those who take the decedent's estate. But where the settlement is a *bona fide* resolution of a truly adversarial dispute as

---

10. Nor are we aware of any federal estate tax requirement or preference for charging administrative expenses to residuary corpus.

11. *Cf. Estate of Wright v. United States,* 677 F.2d 53 (9th Cir. 1982) ("The paramount concern, for federal tax purposes, is with the real distribution of the funds rather than their nominal source," at 54, and, " 'the amount to be deducted for charitable gifts must be computed on the basis of what the charities actually received, not on the basis of what is provided in the will,' " at 55).

to rights of the charity under a will of the decedent, then the foregoing requirement would appear to be satisfied, for in such a case what the charity receives it receives *as a result and by virtue of* the provision made for it in the decedent's will, whether or not it receives precisely what it would be entitled to if no settlement had been made. The contrary conclusion would be necessarily inconsistent with Rev. Rul. 89-31 as well as with such decisions as *Flanagan, Northern Trust Co.,* and *Estate of Strock. See also Dumont's Estate v. C.I.R.* [45-2 USTC ¶ 10,216], 150 F.2d 691, 692-94 (3d Cir. 1945).

We further note that the settlement and Probate Court judgment are wholly valid and binding under Texas law, and under Texas law control the extent to which the administrative expenses are charged to the residuary estate for purposes of computing "the initial net fair market value of the assets constituting" the Trusts. *See Mooney v. Harlin,* 622 S.W.2d 83, 85 (Tex. 1981) (binding nature of Texas Probate Court judgments, which are *in rem*). Texas law has long recognized the "family settlement doctrine." As stated in *Matter of Estate of Hodges,* 725 S.W.2d 265, 267 (Tex. App. — Amarillo, 1986, writ ref'd n.r.e.):

> "A family settlement agreement is an alternative method of administration in Texas that is a favorite of the law. *Salmon v. Salmon,* 395 S.W.2d 29, 32 (Tex. 1965); *Estate of Morris,* 577 S.W.2d 748, 755-56 (Tex. Civ. App. — Amarillo 1979, writ ref'd n.r.e.). The Theory underlying the validity of family settlement is stated in *Pitner v. United States* [68-1 USTC ¶ 12,499], 388 F.2d 651, 656 (5th Cir. 1967):

Appendix D

> 'This approach is made possible by section 37 of the [Texas] Probate Code which provides that when a person dies leaving a will, [. . .] "all of his estate devised or bequeathed by such will shall vest immediately in the devisees or legatees;" [. . .] subject to the payment of the decedent's debts. This provision leaves the beneficiaries of an estate free to arrange among themselves for the distribution of the estate and for the payment of expenses from that estate.' " (Footnote omitted).

See also Cook v. Hamer, 309 S.W.2d 54, 56 (Tex. 1958); *Wade v. Wade,* 167 S.W.2d 1008, 1010 (Tex. 1943); *Everett v. Everett,* 309 S.W.2d 893, 896 (Tex.Civ.App. — Waco 1958, writ ref'd n.r.e.). In *Pitner* we applied the Texas family settlement doctrine in holding that certain postmortem attorneys' fees were deductible for estate tax purposes as administrative expenses under Code § 2053(a)(2). *Pitner v. United States,* 388 F.2d 651 (5th Cir. 1967).

Though the Tax Court in this case specifically refused to make a finding as to whether the agreed allocation of administrative expenses was a settlement of a bona fide dispute, the Commissioner argues precisely this point on appeal. He claims, as he did below, that the settlement, at least as far as it dealt with the allocation of administrative expenses, was collusive and designed simply to avoid payment of taxes, and that the IRS should not now be forced to abide by a settlement in which it had no voice.

We reject the Commissioner's argument. This contention was thoroughly tried below, and, as the Estate points out, the Commissioner never produced any evidence with which to question the character of the proceedings. The Estate, on the other

hand, presented the testimony of Alan Leibel, an attorney who represented Warren's children throughout the litigation in the Probate Court. Leibel testified that the negotiations, on the administrative expense issue as well as others, were protracted and adversarial.

It is indisputably clear that the litigation, and its settlement, were to resolve adversarial, nontax, *bona fide* disputes between the parties.

We also note that the terms of the will provide independent verification of the adversarial interests involved in the probate contest. If all administrative expenses had been taken out of the corpus of the residuary estate so that "the initial net fair market value" of the assets of the Trusts would have been lower, the annuity amount received by the Charities would likewise have been lower. This would have benefited the children and grandchildren because less of the estate would have been paid out to the Charities and more would have been left to them after the twenty-year term of the Trusts.

As calculated by the Commissioner and under the Tax Court's judgment, the annuity payments to the Charities were $878,131 a year, as compared to $1,471,576 per year under the Probate Court's judgment, a difference of $593,445 a year. Over the 20-year term this would amount to $11,868,904 more going to the Charities, and the same amount less being available to Warren's children and grandchildren at the termination of the Trusts (the children and grandchildren receiving nothing from the Trusts prior to their termination).

The Commissioner's brief makes the conclusory assertion that because "[t]he net effect of this allocation of administrative

expenses was to reduce both the federal estate and income tax burdens of the estate" the settlement "was not adverse to the interests of the various parties to" it and hence was not *bona fide* and adversarial. The record simply does not bear this out. The Commissioner's position and that of the Tax court reduced the amount of the estate tax charitable deduction by approximately $6,806,756 from what it would have been had the Probate Court judgment been followed.[12] Even as calculated by the Commissioner, the net taxable estate was only $2,357,320, and so the maximum estate tax rate would have been 49%. Code § 2001(c)(1). Of course, if the Probate Court position were applied, the same estate tax liability as resulted from the Tax Court's judgment could be achieved without using as an estate tax deduction some $6,806,756 (the amount of the decrease in the estate tax charitable deduction) of administrative expenses, which in turn would free that amount up to take as an estate income tax deduction.[13] The maximum income tax rate for estates and trusts during 1983 through 1986 was fifty percent and has been less ever since. Code § 1(e). Consequently, the tax benefits — estate tax and income tax — in regard to the administrative expenses and the estate tax charitable deduction could not have amounted in all to more than half the amount of the difference in the size of the estate tax charitable deduction, or some $3,403,378 (1/2 of $6,806,756). In addition to this tax benefit, there would be, if the Probate Court judgment were followed, the potential for increased annual income tax deductions by the virtue of the increase in the amount of the annual annuity payable to the Charities by $593,445. Even on the

---

12. The $593,445 difference in the annual annuity amount times the appropriate 11.4699 factor (see note 6, *supra*) equals $6,806,756.

13. Under Code § 642(g) an item of administrative expense may not be taken both as an estate tax and as an income tax deduction.

unlikely assumption that there would be sufficient net taxable income to realize the full potential of this increased deduction (in addition to the hypothesized income tax deduction for administrative expenses), over the 20-year term it would not amount to a tax saving of over some $4,255,000.[14] The total of the maximum potential estate and income tax savings from administrative expenses, $3,403,378, plus the maximum potential income tax savings from the increased charitable deduction for increased annuity payments to charity, $4,255,000, would thus be less than $7,660,000. This would still leave more than $4,000,000 ($11,868,904, the pre-tax loss to the children and grandchildren, less $7,660,000 in maximum potential tax savings, the benefit of which could accrue to them on termination of the Trusts) to fight over. That is a substantial sum, and a substantial fraction of the net estate. The Commissioner has presented no calculations whatever to demonstrate what the potential tax savings would be or that they would even approach the amount of the enhancement in the position of the Charities to the detriment of the children and grandchildren.

The record as a whole affirmatively demonstrates that the dispute was a truly adversariel, nontax one and that the parties reached an arms-length and *bona fide* settlement of that dispute

---

14. The top income tax for estates in the years 1983 through 1986 was 50%; in 1987 through 1990 it did not exceed 38.5%; since then it has not exceeded 31%. See Code §1. Assuming 3.6 years (May 27, 1983 through December 1986) at 50%, 4 years at 38.5%, and 12.4 years at 31%, the total income tax savings over the 20 years from the increased income tax charitable deduction would be approximately $4,253,328, calculated as follows:

3.6	x	$593,445	=	$2,136,440.20	x	.50	=	$1,068,220.10
4	x	$593,445	=	$2,373,780	x	.385	=	$ 913,905.30

that was essentially approved by the Probate Court, and that what the Charities received in the settlement and under the Probate Court judgment accrued to them by virtue and as a result of the bequest to them in Article V of the will. There is no substantial evidence in the record to sustain a contrary finding. Consequently, there is no need for a remand to the Tax Court for a fact finding on that issue. We further determine that the settlement and Probate Court decree are valid and binding under Texas law, particularly the Texas family settlement doctrine. In these circumstances, we conclude that the approach of Rev. Rul. 89-31, rather than of *Bosch,* is appropriate, and that the estate tax charitable deduction should be computed on the basis of what the Charities will receive under Article V of the will pursuant to the Probate Court's judgment.

Conclusion

We hold that the estate tax charitable deduction must be computed on the basis of what the Charities will receive under Article V of the will pursuant to the Probate Court's judgment, and that the Tax Court erred in holding to the contrary. We accordingly reverse the judgment of the Tax Court and remand the case to that court for further proceedings consistent herewith, including recalculation of the appropriate estate tax in conformity with our holding.

APPENDIX E — JUDGMENT OF THE UNITED STATES CLAIMS COURT FILED NOVEMBER 29, 1991

IN THE UNITED STATES CLAIMS COURT

No. 540-89 T

JAMES W. BURKE, AS PERSONAL REPRESENTATIVE OF THE ESTATE OF EDNA SPROULL WILLIAMS, DECEASED

v.

THE UNITED STATES

JUDGMENT

Pursuant to the order of November 27, 1991.

IT IS ORDERED AND ADJUDGED this date, pursuant to Rule 58, that the complaint is dismissed. No costs.

David A. Lampen
Clerk of Court
By: s/ Linda A. Eddin
Deputy Clerk

NOTE: As to appeal, 60 days from this date, see RUSCC 72, re number of copies and listing of *all plaintiffs*. Filing fee is $105.00.

[stamped]
RECEIVED
DEC 06 1991

APPENDIX F — ORDER OF THE UNITED STATES CLAIMS COURT FILED NOVEMBER 27, 1991

IN THE UNITED STATES CLAIMS COURT

No. 540-89T

(Filed: November 27, 1991)

JAMES W. BURKE, as Personal Representative of the Estate of EDNA SPROULL WILLIAMS, Deceased

v.

THE UNITED STATES

ORDER

This suit was brought by the personal representative of the estate of Edna Sproull Williams to obtain a refund of $110,717 paid to the defendant United States of America (Government) because of an asserted tax deficiency. The matter is before the court on the Government's motion for summary judgment and on plaintiff's crossmotion for summary judgment under RUSCC 56.

Facts

The following facts are undisputed. Edna Sproull Williams, decedent, died testate on February 28, 1982. At the time of her death, she was a resident of Jacksonville, Duval County, Florida. Plaintiff is the Estate of Edna Sproull Williams, acting by and through James W. Burke as its personal representative.

Decedent executed her last will and testament on October 9,

1979, and a codicil to that will on October 25, 1979. Article I of decedent's will states in pertinent part:

> I DIRECT THAT ALL MY JUST DEBTS,INCLUDING EXPENSES OF MY LAST ILLNESS AND FUNERAL EXPENSES BE PAID BY MY PERSONAL REPRESENTATIVES AS SOON AS REASONABLY CONVENIENT AFTER MY DEATH. I DIRECT THAT ALL ESTATE, INHERITANCE AND SUCCESSION TAXES THAT MAY BE LEVIED AGAINST MY ESTATE, INCLUDING SUCH TAXES LEVIED AGAINST PROPERTY CONSTITUTING ANY PART OF MY ESTATE FOR FEDERAL ESTATE TAX PURPOSES, WHETHER PASSING UNDER THIS WILL OR OTHERWISE, SHALL BE PAID BY MY PERSONAL REPRESENTATIVES SOLELY OUT OF THE RESIDUARY ESTATE BEQUEATHED HEREUNDER, IT BEING MY INTENTION THAT THE PORTION OF MY ESTATE DEVISED AND BEQUEATHED TO OR FOR THE BENEFIT OF ALL LEGATEES, SHALL BE ENJOYED BY THEM FREE FROM ANY BURDEN FOR SUCH ESTATE, INHERITANCE OR SUCCESSION TAXES * * *.

With regard to the residue of her estate, decedent's will at Article XIII states in pertinent part:

> I GIVE, DEVISE AND BEQUEATH ALL OF

Appendix F

THE REST RESIDUE AND REMAINDER OF MY ESTATE, INCLUDING ALL LAPSED LEGACIES OR DEVISES, AFTER PAYING TEEREFROM ANY DEBTS AND TAXES, AND OTHER OBLIGATIONS OF MY ESTATE, INCLUDING ALL ADMINISTRATION EXPENSES, TO THE TRUSTEES OF THE EDNA SPROULL WILLIAMS FOUNDATION * * *.

The Edna Sproull Williams Foundation was created during decedent's lifetime under a Trust Agreement dated February 13, 1976 and is an organization exempt from taxation under section 501(c)(3).

On November 11, 1982, the personal representatives filed a Petition for the Construction of the Will of Decedent Edna Sproull Williams with the Probate Division of the Circuit Court of Duval County, Florida. In this petition, the representatives argued, *inter alia,* that although Article I of decedent's will mandates that estate taxes be paid out of the residuary estate, Article XIII implies no such mandate as to administration expenses and should be interpreted to mean that such expenses may be paid out of the residuary estate, at the discretion of the Personal Representatives, if not paid out of income.

On November 12, 1982 the Circuit Court of Duval County, Florida issued an order stating that Articles I and XIII of decedent's will are construed to authorize payment of administration expenses by the personal representatives out of income if they choose to do so and if they choose not to pay administration costs out of income, such expenses shall be paid out of the residual estate.

Appendix F

On November 24, 1982, the personal representatives filed the U.S. Estate Tax Return for the Estate of Edna Sproull Williams. The estate tax return reported a total gross estate of $10,489,753.94 and total deductions of $9,747,444.42, leaving a net taxable estate of $742,309.52. Of the $9,747,444.42 in deductions on the estate tax return, $9,662,605.10 represented "Charitable, Public, and Similar Gifts and Bequests" to the Edna Sproull Williams Foundation. Of this amount, $8,869,080.10 represented the claimed charitable residuary bequest.

No deduction for administration expenses was taken from the gross estate. Instead of deducting the administration costs on the estate tax return, the personal representatives elected to deduct them on the estate's income tax return, filed April 5, 1983. The deduction claimed for administration expenses totalled $144,441. There is a dispute between the parties regarding the source from which the administration expenses were paid. Plaintiff contends these expenses were paid out of post-mortem income; defendant contends that plaintiff has not proven his factual contention that these expenses were paid out of post-mortem income and not from principal.

The Commissioner conducted an audit of the estate tax return and determined that the $144,441 of administration expenses should reduce the amount of the charitable bequest passing to the charitable foundation. As a result the charitable deduction claimed by the estate for the bequest of the residue to the Edna Sproull Williams Foundation was reduced by $236,536.38 (from $9,662,605.10 to $9,426,068.72) with a resulting tax deficiency of $80,110.87 (plus $30,606.13 interest). This amount was paid in full under protest on July 9, 1985.

On October 24, 1986, plaintiff filed a Claim for Refund, which

was disallowed on October 7, 1987. Plaintiff filed a complaint with this court on October 4, 1989.

In its motion for summary judgment, defendant contends that under the decedent's will and Florida law the administration expenses of the estate are pre-residue expenses. Plaintiff contends that the decedent's will does not mandate that administration expenses be paid out of pre-residue principal and that the residue of the estate was increased by paying administration expenses out of post-mortem income rather than from the principal of the estate. The sole issue for decision is whether the charitable bequest deduction claimed by the Estate of Edna Sproull Williams must be reduced by the amount of the administration expenses deducted from the estate's income tax returns.

OPINION

Summary Judgment Standards

Summary judgment is appropriate when there are no genuine issues of material fact in dispute and the moving party is entitled to judgment as a matter of law. RUSCC 56(c). Only disputes over material facts, or facts that might significantly affect the outcome of the suit under governing law, preclude an entry of judgment. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248 (1986). A dispute about a material fact is genuine if the evidence would permit a reasonable juror to return a verdict in favor of the nonmovant. *Id.* The moving party has the burden of establishing that there are no genuine material issues in dispute and that the movant is entitled to judgment as a matter of law. *Celotex Corp. v. Catrett*, 477 U.S. 317, 322-23 (1986). A nonmoving party has the burden of providing sufficient evidence, not necessarily admissible at trial, to show that a genuine issue of material fact

indeed exists as to an essential element of its case with respect to which it has the burden of proof. *Celotex*, 477 U.S. at 322-24. In resolving the motion, the court cannot weigh the evidence and determine the truth of the matter on summary judgment. *Anderson*, 477 U.S. at 249, 255. Any evidence presented by the opponent is to be believed, and all justifiable inferences are to be drawn in its favor. *Id.* at 255.

Deductibility of Administration Expenses

I.R.C. § 2001(a) imposes an estate tax on the transfer of the taxable estate of every decedent who is a citizen of the United States. The taxable estate is equal to the gross estate less certain deductions permitted under I.R.C. §§ 2053-2056.

In general, § 2055 allows an estate a deduction for the amount of all bequests to charity to the extent that the transferred property is required to be included in the gross estate. The estate is entitled to deduct only the amount actually passing to the charitable beneficiary.[1] *Estate of Edyth Bush v. United States*, 223 Ct. Cl. 161, 618 F.2d 741 (1980); *Harrison v. Northern Trust Co.*, 317 U.S. 476, 480 (1943). Plaintiff bears the burden of showing a right to the claimed deduction. *Interstate Transit Lines v. Commissioner*, 319 U.S. 590, 593 (1943).

The decedent's estate realized a total income for the period ending December 31, 1982 in the amount of $434,515. Income received by an estate during its administration (post-mortem income) is not part of the gross estate of the decedent for estate tax

---

1. I.R.C. § 2055(d) limits the amount of the charitable deduction: "The amount of the deduction under this section for any transfer shall not exceed the value of the transferred property required to be included in the gross estate."

purposes and is not taxable as such. *Bowes v. United States,* 593 F.2d 272, 275 (7th Cir. 1979); *Connecticut Bank & Trust Co. v. United States,* 465 F.2d 760, 764-65 (2d Cir. 1972); *Alston v. United States,* 349 F.2d 87, 88-89 (5th Cir. 1965). Instead, post-mortem income is taxable to the estate itself as income. I.R.C. § 641(a)(3). Because it is not includable in the gross estate, post-mortem estate income may not be used to increase the charitable deduction. *Bowes v. United States,* 593 F.2d 272, 275 (7th Cir. 1979).

Accepting plaintiff's position, for the purpose of these dispositive motions that the administration expenses were paid out of post-mortem income in order not to decrease the residue of the estate going to the charitable foundation, does not change the fact that the consequence of such action was to increase the amount of the charitable deduction. If administration expenses were paid from pre-residue estate assets, the residue and the charitable deductions would be reduced by that amount. Thus, post-mortem income was indirectly used to increase the charitable deduction by the amount of the administration expenses.

Generally, the residue of an estate is defined as that which remains after the payment of charges, debts and bequests. *See, e.g., Estate of Edyth Bush v. United States, supra,* 223 Ct. Cl. at 169, 618 F.2d at 745. The devolution of property in the estate and, thus, the amount of the residue remaining and qualifying for the charitable deduction is a question of state law. *Riggs v. Del Drago,* 317 U.S. 95 (1942); *Harris v. United States*, 370 F.2d 887, 893 (4th Cir. 1966); *Estate of Short v. Commissioner,* 68 T.C. 184, 190 1977). In the instant case, FLORIDA STAT. ANN., § 738.05(1) (WEST 1979), provides in pertinent part:

UNLESS THE WILL OTHERWISE

Appendix F

> PROVIDES * * * ALL EXPENSES INCURRED IN CONNECTION WITH THE SETTLEMENT OF A DECEDENT'S ESTATE, INCLUDING DEBTS, FUNERAL EXPENSES, ESTATE AND OTHER DEATH TAXES, INTEREST AND PENALTIES CONCERNING SUCH TAXES, FAMILY ALLOWANCES, FEES OF ATTORNEYS AND PERSONAL REPRESENTATIVES, AND COURT COSTS SHALL BE CHARGED AGAINST THE PRINCIPAL OF THE ESTATE.

In the instant case, there is no conflict between the Florida statute and the testator's will because the will did, in fact, provide for the payment of administration expenses out of pre-residue principal. Article XIII of the will stated:

> I GIVE, DEVISE AND BEQUEATH ALL OF THE *REST RESIDUE AND REMAINDER OF MY ESTATE*, INCLUDING ALL LAPSED LEGACIES OR DEVISES, *AFTER PAYING THEREFROM ANY DEBTS AND TAXES, AND OTHER OBLIGATIONS OF MY ESTATE, INCLUDING ALL ADMINISTRATION EXPENSES*, TO THE TRUSTEES OF THE EDNA SPROULL WILLIAMS FOUNDATION.

(Emphasis added.)

The plain language of Article XIII indicates that the testator intended that the administration expenses be paid out of the residue

of her estate. A different interpretation may not be given to the words expressed in a will unless there is an ambiguity or unless a contrary intention clearly appears. A court must assume that the testatrix meant what she said in the will. *See, e.g., Floyd v. Smith,* 59 Fla. 485, 51 So. 537 (1910); *Lowrimore v. First Savings & Trust Co. of Tampa,* 102 Fla. 740, 140 So. 887, 891 (1931); *Mosgrove v. Mach,* 133 Fla. 459, 182 So. 786 (1938). Here, there is no ambiguity or uncertainty obscuring the intent of the testatrix. Reading Articles I and XIII together, it is apparent that she bequeathed the residue of her estate to the Foundation free of any debts, taxes or other obligations. To this aim, she provided all debts, taxes and obligations, including administration expenses, be paid out of the principal of her estate before the remainder was transferred to the charitable foundation.

Throughout a series of cases beginning with *Waldrop v. United States,* 133 Ct. Cl. 902, 137 F.Supp. 753 (1956), the federal courts have read the estate laws as requiring that taxes and administration expenses charged against a charitable residual legacy must be deducted in full from the amount of the legacy at death in computing the charitable deduction. The Fifth Circuit decision in *Alston v. United States,* 349 F.2d 87 (5th Cir. 1965), is directly on point. In *Alston,* the decedent, by his will, after certain specific bequests to nieces and nephews, left the residue of his estate to a qualified charitable foundation. Unlike decedent's will in the instant case, the will in *Alston* did not specify the source from which the testator's debts and expenses must be paid. The estate's executor's elected to deduct certain administration expenses on the estate's income tax return. The amount claimed as a charitable deduction was not reduced by these administration expenses deducted on the income tax return. The Commissioner asserted an estate tax deficiency based on the failure to deduct these administration expenses from the gross estate in computing the residue.

Appendix F

The Fifth Circuit looked to Georgia law which provided that, unless otherwise directed by the will, the debts of the testator including the expenses of administration should be paid out of the residue of the estate. *Alston v. United States, supra,* 349 F.2d at 89. The taxpayers in *Alston* argued that if the administration expenses are paid out of post-mortem income rather than the estate's corpus, the residue passing to the charitable foundation is not decreased by said expenses. *Id.* In support of this argument, the taxpayers cited two cases, *Estate of Luehrmann,* 287 F.2d 10 (8th Cir. 1961) and *Republic National Bank of Dallas v. Commissioner,* 334 F.2d 348 (5th Cir. 1964). However, the court in *Alston* found that in neither of these cases was the question reached, since in each case the court found no proof that the administration expenses in issue had in fact been paid from income.

In holding for the Commissioner that administration expenses were pre-residue, the court based its decision on the clear language of the Georgia statute cited above and related Georgia decisions. 349 F.2d at 90. The reasoning of the *Alston* case has been followed by other courts considering the same issue. *See, Rifkind v. United States,* 5 Cl. Ct. 362, 373-74 (1984); *Estate of Horn v. Commissioner,* 91 T.C. 100 (1988); Rev. Rul. 73-98, 1973-1 Cum. Bull. 407; Rev. Rul. 82-6, 1982-1 Cum. Bull. 137.

In its cross-motion, plaintiff notes the decision of the Florida Circuit Court, which found that Article I and Article XIII of decedent's will can be construed to authorize payment of administration expenses out of post-mortem income or out of pre-residue principal, at the choice of the personal representatives. However, as plaintiff correctly points out, this court is not bound by the judgment of the Florida Circuit Court. That court is not the highest court of the state of Florida. *Commissioner v. Estate of Bosch,* 387 U.S. 456, 465 (1967); *Estate of Harmon v. Commissioner,* 84 T.C. 329, 333 (1985).

Appendix F

It is clear that under the Florida statute and under the terms of decedent's will, the administration costs are to be charged against the principal of the estate. This reduces that amount of the residue to be received by the charitable foundation under decedent's will. Therefore, the estate's charitable deduction must also be reduced by the amount of the administration expenses. *Harrison v. Northern Trust Co., supra,* 317 U.S. at 480.

The emphasis that plaintiff places on the payment of administration expenses from post-mortem income instead of principal is misplaced. The fact remains that 1) post-mortem income cannot be used to increase the amount of a charitable residual legacy, even by indirectly increasing the amount in the residual bequest; and 2) under both Florida state law and the unambiguous terms of decedent's will, these expenses should have been paid out of preresidue principal. Any increase in the amount of the residue passing to charity as a result of the use of estate post-mortem income to pay administration expenses cannot be included in the charitable deduction.

Accordingly, for all the foregoing reasons, the defendant is entitled to judgment as a matter of law. Therefore, it is ORDERED that defendant's motion for summary judgment is hereby granted, plaintiff's cross-motion for summary judgment is denied, and final judgment shall be entered dismissing the complaint with no costs to be assessed.

s/ James F. Merow
James F. Merow
Judge

APPENDIX G — INTERNAL REVENUE CODE SECTION 2055(a)

SEC. 2055. TRANSFERS FOR PUBLIC, CHARITABLE, AND RELIGIOUS USES.

[Sec. 2055(a)]

(a) In General. — For purposes of the tax imposed by section 2001, the value of the taxable estate shall be determined by deducting from the value of the gross estate the amount of all bequests, legacies, devises, or transfers —

(1) to or for the use of the United States, any State, any political subdivision thereof, or the District of Columbia, for exclusively public purposes;

(2) to or for the use of any corporation organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, including the encouragement of art, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), and the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private stockholder or individual, which is not disqualified for tax exemption under section 501(c)(3) by reason of attempting to influence legislation, and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office;

(3) to a trustee or trustees, or a fraternal society, order, or association operating under the lodge system,

but only if such contributions or gifts are to be used by such trustee or trustees, or by such fraternal society, order, or association, exclusively for religious, charitable, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals, such trust, fraternal society, order, or association would not be disqualified for tax exemption under section 510(c)(3) by reason of attempting to influence legislation, and such trustee or trustees, or such fraternal society, order or association, does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office; or

(4) to or for the use of any veterans' organization incorporated by Act of Congress, or of its departments or local chapters or posts, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

For purposes of this subsection, the complete termination before the date prescribed for the filing of the estate tax return of a power to consume, invade, or appropriate property for the benefit of an individual before such power has been exercised by reason of the death of such individual or for any other reason shall be considered and deemed to be a qualified disclaimer with the same full force and effect as though he had filed such qualified disclaimer. Rules similar to the rules of section 501(j) shall apply for purposes of paragraph (2).

FILED
NOV 4 1993
OFFICE OF THE CLERK

No. 93-339

In the Supreme Court of the United States

OCTOBER TERM, 1993

JAMES W. BURKE, AS PERSONAL REPRESENTATIVE OF THE ESTATE OF EDNA SPROULL WILLIAMS, DECEASED, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

DREW S. DAYS, III
Solicitor General

MICHAEL L. PAUP
Acting Assistant Attorney General

GILBERT S. ROTHENBERG
JOAN I. OPPENHEIMER
Attorneys

Department of Justice
Washington, D.C. 20530
(202) 514-2217

BEST AVAILABLE COPY

QUESTION PRESENTED

Whether the charitable deduction claimed on the decedent's estate tax return must be reduced by the amount of the estate's administrative expenses.

TABLE OF CONTENTS

	Page
Opinions below	1
Jurisdiction	1
Statement	2
Argument	5
Conclusion	12

TABLE OF AUTHORITIES

Cases:

Alston v. *United States*, 349 F.2d 87 (5th Cir. 1965)	5, 6, 7
Ballantine v. *Tomlinson*, 293 F.2d 311 (5th Cir. 1961)	7
Bowes v. *United States*, 593 F.2d 272 (7th Cir. 1979)	6, 8
Commissioner v. *Estate of Bosch*, 387 U.S. 456 (1967)	4, 8
Connecticut Bank & Trust Co. v. *United States*, 465 F.2d 760 (2d Cir. 1972)	6
Estate of Horne v. *Commissioner*, 91 T.C. 100 (1988)	7
Estate of Luehrmann v. *Commissioner*, 287 F.2d 10 (8th Cir. 1961)	11
Estate of Street v. *Commissioner*, 974 F.2d 723 (6th Cir. 1992), rev'g in part 56 T.C.M. (CCH) 774 (1988)	7, 11
Estate of Warren v. *Commissioner*, 981 F.2d 776 (5th Cir. 1993)	5, 9, 10
Estate of Wright v. *United States*, 677 F.2d 53 (9th Cir.), cert. denied, 459 U.S. 909 (1982)	11
Harrison v. *Northern Trust Co.*, 317 U.S. 476 (1943)	10
Morgan v. *Commissioner*, 309 U.S. 78 (1940)	9
Oetting v. *United States*, 712 F.2d 358 (8th Cir. 1983)	11
Rifkind v. *United States*, 5 Cl. Ct. 362 (1984)	7

Statutes:

Act of Oct. 29, 1992, Pub. L. No. 102-572, § 902(a), 106 Stat. 4516	1

Statutes—Continued:

	Page
Internal Revenue Code of 1954 (26 U.S.C.):	
§ 641(a)(3)	6
§ 642(c)	6, 8
§ 642(c)(2)	11
§ 2001(a)	6
§ 2031(a)	4, 6
§ 2051	4, 6
§ 2053	4
§ 2053(a)	6
§ 2053(a)(2)	6
§§ 2053-2056	6
§ 2055	6, 8
§ 2055(d)	6, 8
§ 2055(e)(2)	11
§ 2056	6
Fla. Stat. Ann. (West 1991):	
§ 733.608	9
§ 738.05(1)	4, 9

Miscellaneous:

4 J. Rabkin & M. Johnson, *Federal Income, Gift and Estate Taxation* (1992)	7
S. Rep. No. 1013, 80th Cong., 2d Sess. Pt. 2 (1948)	7

In the Supreme Court of the United States

OCTOBER TERM, 1993

No. 93-339

JAMES W. BURKE, AS PERSONAL REPRESENTATIVE OF THE ESTATE OF EDNA SPROULL WILLIAMS, DECEASED, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 3a-17a) is reported at 994 F.2d 1576. The opinion of the Court of Federal Claims (Pet. App. 41a-51a) is unreported.[1]

JURISDICTION

The judgment of the court of appeals was entered on June 2, 1993. The petition for a writ of certiorari was filed on August 31, 1993. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

---

[1] Congress changed the name of the United States Claims Court to the United States Court of Federal Claims effective October 29, 1992. Pub. L. No. 102-572, § 902(a), 106 Stat. 4516.

STATEMENT

1. Edna Sproull Williams, who was a Florida resident, died on February 28, 1982 (Pet. App. 4a). She bequeathed most of her substantial estate to the Edna Sproull Williams Foundation, a tax-exempt, charitable organization (*id.* at 43a-44a). Article XIII of decedent's will provides (Pet. App. 5a):

> I give, devise and bequeath all of the rest, residue and remainder of my estate, including all lapsed legacies or devises, after paying therefrom any debts and taxes, including estate, inheritance or succession taxes, and other obligations of my estate, including all administration expenses, to the Trustees of the EDNA SPROULL WILLIAMS FOUNDATION.

Article I of her will directs her estate, inheritance, and succession taxes to be paid solely from the residuary estate (Pet. App. 5a).

On November 11, 1982, petitioner filed a petition for will construction in the Florida probate court seeking a determination under Florida law that decedent's will authorizes the payment of administrative expenses from the estate's post-mortem income, rather than from its principal (Pet. App. 4a). On November 12, 1982—the day after the unopposed petition for construction was filed—the Florida probate court entered an order granting the requested relief and permitting payment of administrative expenses either from income or from the residuary estate, at petitioner's discretion (*id.* at 5a-6a).

On November 24, 1982, petitioner filed the estate's federal estate tax return in which he valued the gross estate at $10,489,753.94 and claimed total deductions of

$9,747,444.42, leaving a taxable estate of $742,309.52. The claimed deductions included charitable deductions totaling $9,662,605.10, of which $8,869,080.10 represented the residuary bequest to the Foundation (Pet. App. 6a). Petitioner did not deduct the administrative expenses, which totaled $144,441, on the estate tax return. *Ibid.* Instead, he elected to deduct them on the estate's income tax return filed April 5, 1983, on the asserted ground that they were paid from post-mortem income (*id.* at 44a).

The estate was administered for seven years, during which time it earned substantial income (Pet. App. 13a). That income augmented the residuary bequest of $8,869,080 (Pet. 10), and the Foundation eventually received total distributions of $10,091,707 (*ibid.*).

On audit, the Internal Revenue Service determined that the administrative expenses claimed as a deduction on the estate's income tax return instead should have been shown on its estate tax return as reducing the charitable deduction of $8,869,080.10 for the residuary bequest to the Foundation. This adjustment reduced the charitable deduction on the estate tax return by $236,536.38—the amount of the administrative expenses plus the estate taxes attributable thereto. The Service therefore assessed an estate tax deficiency of $80,110.87 (Pet. App. 6a-7a).

Petitioner paid the deficiency, plus interest, and commenced this refund suit (Pet. App. 7a, 51a).

2. The parties submitted the case to the trial court on cross-motions for summary judgment. The trial court accepted, for purposes of the motions, petitioner's claim that the administrative expenses were paid from post-mortem income. The court determined,

however, that the charitable deduction had to be reduced by the amount paid for administrative expenses from post-mortem estate income because, under federal law, "post-mortem estate income may not be used to increase the charitable deduction" (Pet. App. 47a). The court further held (i) that administrative expenses must be charged to principal under the terms of the will and under Florida law (Fla. Stat. Ann. § 738.05(1) (West 1991)) (Pet. App. 47a-51a) and (ii) that, under *Commissioner* v. *Estate of Bosch*, 387 U.S. 456 (1967), the Florida probate court order is not binding in determining the requirements of the federal estate tax (Pet. App. 50a). The court therefore granted the government's motion for summary judgment (*id.* at 51a).

3. The court of appeals affirmed. The court held that the proper characterization of administrative expenses under the federal estate tax is an issue controlled by federal, not state, law (Pet. App. 9a-10a & n.5). The court concluded that, under the federal estate tax (Pet. App. 12a):

> when a decedent dies, a finite amount known as the gross estate is legally created. Any deductions for expenses incurred in administering the estate are theoretically derived from this amount and, regardless of the actual source of payment, must be accounted for within the gross estate.

The court noted that the term "gross estate" is defined as "the value *at the time of death* of all [decedent's] property" (Pet. App. 10a, quoting 26 U.S.C. 2031(a)). The term "taxable estate" is the "gross estate" less allowed deductions (Pet. App. 11a, citing 26 U.S.C. 2051, 2053).

The court noted that, in computing the charitable deduction for the estate tax, the relevant inquiry is the amount received by the charity from the gross estate. The additional sums thereafter distributed to the Foundation from post-mortem income represent charitable deductions for the estate's *income* tax, not for the estate tax itself—and the estate had already received a charitable deduction for the distributions from post-mortem income on its federal income tax returns (Pet. App. 13a-14a).

The court distinguished the present case from *Estate of Warren* v. *Commissioner*, 981 F.2d 776 (5th Cir. 1993), which held that the Tax Court was bound by a state probate court's judgment that 72 1/2% of the administrative expenses were chargeable to post-mortem income (Pet. App. 14a-16a). The court of appeals noted that in *Warren* the state probate court judgment "resulted from a bona fide adversarial proceeding between the various beneficiaries under the will," while here "there was no *bona fide* adversarial proceeding leading to the Florida probate court's decision" (Pet. App. 16a). The court further noted that state court decisions cannot bind federal courts in the interpretation of federal estate tax provisions and that, if *Warren* were interpreted to hold to the contrary, it would be inconsistent with prior decisions from that same circuit (Pet. App. 17a, citing *Alston* v. *United States*, 349 F.2d 87 (5th Cir. 1965)).

ARGUMENT

The decision of the court of appeals is correct and does not conflict with any decision of this Court or any other court of appeals. Further review is therefore not warranted.

1. Administrative expenses are charges against the gross estate regardless of the source for their payment. The federal estate tax is imposed on "the transfer of the taxable estate." 26 U.S.C. 2001(a). Under Section 2051, the taxable estate is defined as the gross estate less the deductions permitted by Sections 2053-2056.[2] In particular, Section 2053(a) provides that "the value of the taxable estate shall be determined by deducting from the value of the gross estate such * * * administration expenses * * * as are allowable by the laws of the jurisdiction * * * under which the estate is being administered." 26 U.S.C. 2053(a). The gross estate includes "the value *at the time of* * * * *death* of all property, real or personal, tangible or intangible, wherever situated." 26 U.S.C. 2031(a) (emphasis added).

Under Section 2055(d), the amount of a charitable deduction is limited to "the value of the transferred property required to be included in the gross estate." 26 U.S.C. 2055(d). Income received by an estate during its administration ("post-mortem income") is *not* included in the gross estate for estate tax purposes. *Bowes* v. *United States*, 593 F.2d 272, 275 (7th Cir. 1979); *Connecticut Bank & Trust Co.* v. *United States*, 465 F.2d 760, 764-765 (2d Cir. 1972); *Alston* v. *United States*, 349 F.2d 87, 88 (5th Cir. 1965). Instead, post-mortem income is includable in the estate's gross income on its income tax return. 26 U.S.C. 641(a)(3). Various deductions are permitted on the fiduciary income tax return, including a deduction for distributions to charity. 26 U.S.C. 642(c).

[2] The deductions from the gross estate include administrative expenses (Section 2053(a)(2)), charitable bequests (Section 2055) and bequests to the surviving spouse (Section 2056).

Under these provisions, the courts and commentators have generally agreed that the charitable deduction (and the similarly framed marital deduction) must be reduced by the amount of administrative expenses, even if these expenses are paid from post-mortem income. *Estate of Street* v. *Commissioner*, 974 F.2d 723, 728 (6th Cir. 1992) ("marital deduction must be reduced in light of any administrative expenses paid from principal or income"), rev'g in part 56 T.C.M. (CCH) 774 (1988); *Alston* v. *United States*, 349 F.2d at 88 (administration expenses must be deducted from the gross estate even though paid out of post-mortem income); *Ballantine* v. *Tomlinson*, 293 F.2d 311, 313 (5th Cir. 1961); *Estate of Horne* v. *Commissioner*, 91 T.C. 100 (1988); *Rifkind* v. *United States*, 5 Cl. Ct. 362, 374 (1984). See also 4 J. Rabkin & M. Johnson, *Federal Income, Gift and Estate Taxation* § 59.07, at 5985 (1992). Congress expressly considered, and rejected, the suggestion that an estate should be allowed to increase the marital deduction by using estate income to pay claims against the estate (S. Rep. No. 1013, 80th Cong., 2d Sess. Pt. 2, at 6 (1948) (emphasis added)):

> The interest passing to the surviving spouse from the decedent is only such interest as the decedent can give. If the decedent by his will leaves the residue of his estate to the surviving spouse and she pays, or *if the estate income is used to pay, claims against the estate so as to increase the residue*, such increase in the residue is acquired by purchase and not by bequest. Accordingly, the value of any such additional part of the residue passing to the surviving spouse can

not be included in the amount of the marital deduction.

2. The court of appeals correctly rejected petitioner's contention that the charitable deduction under Section 2055 should be based upon the actual distributions to the Foundation and that the IRS erred in reducing the deduction by the administrative expenses. The amount of the total assets ultimately transferred to charity from post-mortem income is irrelevant to the amount of the estate tax charitable deduction. The amount of the charitable deduction on the estate tax return depends only on the actual amount passing to charity from assets included in the gross estate. See 26 U.S.C. 2055(d); *Bowes* v. *United States*, 593 F.2d at 275 (decedent's estate cannot increase its charitable deduction by gifts from post-mortem income passing to charity).

For gifts to charity from post-mortem income, a charitable deduction is permitted on the fiduciary *income* tax return. 26 U.S.C. 642(c). As the court of appeals correctly determined, "[t]hat the charitable donation was augmented by post-mortem income, resulting in an overall charitable donation of an amount greater than the estate tax deduction claimed, does not increase the amount of the charitable bequest under the will" (Pet. App. 13a).

3. The court of appeals did not err in disregarding the unopposed Florida probate court order that allowed petitioner to pay administrative expenses from post-mortem income. The proper accounting of administrative expenses on a federal estate tax

return is a question of federal law, not state law.[3] See *Morgan* v. *Commissioner*, 309 U.S. 78, 80-81 (1940). As this Court has observed, "when the application of a federal statute is involved, the decision of a state trial court as to an underlying issue of state law should *a fortiori* not be controlling." *Commissioner* v. *Estate of Bosch*, 387 U.S. at 465. Under the applicable federal law, as the court of appeals correctly noted (Pet. App. 8a-9a), the ultimate source of payment for administrative expenses is not pertinent to the estate tax charitable deduction: "regardless of the source of payments for administrative expenses, such payments are charges against the gross estate and must be accounted for accordingly" (*id.* at 12a).

4. The decision in this case does not conflict with *Estate of Warren* v. *Commissioner*, 981 F.2d 776 (5th Cir. 1993). Under the decedent's will in *Warren*, the charities were to receive annuities for 20 years at the rate of 8 1/2% of the initial fair market value of the trust assets. The charities litigated with the remaindermen in state probate court over the source for payment of the administrative expenses. The parties ultimately settled the suit. The stipulated final judgment provided that 27 1/2% of the administrative expenses would be charged to the estate's corpus and the balance would be charged to residuary post-mortem income. In a suit by the estate challenging the Commissioner's determination of an estate tax

[3] In any event, Florida law is not to the contrary. Although it permits the personal representative to use all the estate's assets, including post-mortem income, to pay its debts, it expressly requires administrative expenses to be charged to estate principal. See Fla. Stat. Ann. §§ 733.608, 738.05(1) (West 1991).

deficiency, the Fifth Circuit held that the Tax Court was bound by the state court judgment and that the charitable donation claimed on the estate tax return was to be reduced by 27 1/2% (and not 100%) of the administrative expenses. The Fifth Circuit concluded that the general rule—that a state probate court decision is not controlling in the characterization of items under the federal estate tax—only applies when the probate court's decision resulted from nonadversarial proceedings and does not apply when "the litigation, and its settlement, were to resolve adversarial, nontax, *bona fide* disputes between the parties." *Id.* at 783. As the court of appeals concluded here, however, the analysis of *Warren* does not apply to this case, for it is undisputed that "there was no *bona fide* adversarial proceeding leading to the Florida probate court's decision" (Pet. App. 16a).

Moreover, in *Estate of Warren*, the court further emphasized that "for purposes of section 2055 what is received [as a charitable gift from the estate] must be received *from the decedent*, and not merely from those who take the decedent's estate" (981 F.2d at 782). While the settlement in *Estate of Warren* determined the amount that the charities received "from the decedent," in the present case, the increased monies received by the charity were unquestionably attributable to post-mortem income and not to the decedent's estate (Pet. App. 13a). There is thus no conflict between the decision in *Estate of Warren* and the decision in this case.

5. The other cases on which petitioner relies (Pet. 11-15) also do not conflict with the decision in this case. In *Harrison* v. *Northern Trust Co.*, 317 U.S. 476, 480 (1943), this Court held that the charitable

deduction is reduced by the amount of the federal estate taxes because payment of the taxes reduces the amount actually passing from the decedent to charity. In *Estate of Luehrmann* v. *Commissioner*, 287 F.2d 10, 16 (8th Cir. 1961), the court of appeals noted that "[t]he record is completely silent as to the source of the funds used to pay the administration expenses" and sustained the Commissioner's position that the charitable deduction is reduced by those expenses. In *Estate of Street* v. *Commissioner*, the court held that the marital deduction is reduced by administrative expenses paid from either principal or income, but not by interest expense on inheritance and estate taxes. 974 F.2d at 728. Interest expense is treated differently because it accrues after death; estate income used to pay that expense therefore would not affect the size of the gross estate. *Ibid.* Finally, *Estate of Wright* v. *United States*, 677 F.2d 53 (9th Cir.), cert. denied, 459 U.S. 909 (1982), and *Oetting* v. *United States*, 712 F.2d 358 (8th Cir. 1983), addressed issues that are not presented in this case. *Estate of Wright* involved the deductibility under 26 U.S.C. 642(c)(2) of payments to charity on the estate's *income* tax return. And, *Oetting* involved the deductibility of amounts given to charity without regard to the rules of Section 2055(e)(2) for split-interest bequests. The decisions in those cases do not create a conflict with the decision in this case.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

DREW S. DAYS, III
Solicitor General

MICHAEL L. PAUP
Acting Assistant Attorney General

GILBERT S. ROTHENBERG
JOAN I. OPPENHEIMER
Attorneys

NOVEMBER 1993

SUPREME COURT, U.S.
FILED
NOV 22 1993
OFFICE OF THE CLERK

No. 93-339

In The

Supreme Court of the United States

October Term, 1993

JAMES W. BURKE, as Personal Representative of the ESTATE OF EDNA SPROULL WILLIAMS, Deceased,

Petitioner,

vs.

THE UNITED STATES,

Respondent.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Federal Circuit

REPLY BRIEF FOR PETITIONER

WILLIAM R. FRAZIER
Counsel of Record
FRAZIER & FRAZIER
Attorneys for Petitioner
1515 Riverside Avenue
Suite A
Jacksonville, FL 32204
(904) 353-5616

COCKLE LAW BRIEF PRINTING CO., (800) 225-6964
OR CALL COLLECT (402) 342-2831

BEST AVAILABLE COPY

TABLE OF CONTENTS

Page

Preliminary Statement 1

Argument 2

Conclusion 9

TABLE OF CITATIONS

Cases Cited:

Estate of Dorothy J. Warren, Dec. v. Commissioner of Internal Revenue, 981 F.2d 776 (5th Cir. 1993) .. 1, 3, 5, 9

Estate of Gordon P. Street v. Commissioner, 974 F.2d 723 (6th Cir. 1992).....5, 6, 7, 8

Estate of Otis C. Hubert, Dec. v. Commissioner, T.C. Docket No. 22333-90, 101 T.C. No. 22, filed October 19, 1993 .....6, 7, 8

Estate of Frances Blow Allen v. Commissioner, T.C. Docket No. 309-91, 101 T.C. No. 23, filed October 20, 1993 8

Statutes Cited:

Internal Revenue Code of 1954:

Section 2053(a) 2

Section 2055 .....1, 2, 4, 6

Section 2056 1

TABLE OF CITATIONS – Continued

Page

Other Authority Cited:

Treasury Regulations

Section 20.2056(b)-4(a) 7

APPENDIX

Appendix A – Opinion of Majority of United States Tax Court in Case of *Estate of Otis C. Hubert, Dec. v. Commissioner*, T.C. Docket 22333-90, 101 T.C. No. 22, filed October 19, 1993 ..... 1a

Appendix B – Commerce Clearinghouse Digest, *Federal Estate and Gift Tax Reports*, reporting of Decision of United States Tax Court in Case of *Estate of Frances Blow Allen v. Commissioner*, T.C. Docket No. 309-91, 101 T.C. No. 23, filed October 20, 1993 .... 30a

PRELIMINARY STATEMENT

Petitioner, in filing the Petition for a Writ of Certiorari with the Court and in connection with the Respondent's Brief in Opposition and this Brief in reply, is fully cognizant of the fact that the primary focus of the Petition is not to discuss in any details the merits or demerits of Petitioner's case or the Opinion of the Court of Appeals, but instead to focus and call to the attention of the Court and its personnel that the basis for jurisdiction of the Supreme Court is to resolve what we believe to be an absolute and irreconcilable conflict between the Opinion of the Fifth Circuit in *Estate of Dorothy J. Warren, Dec. v. Commissioner*, 981 F.2d 776 (5th Cir. 1993) and the decision of the Court of Appeals.

The issue involved is to whether or not a taxpayer is required to reduce the amount of a charitable deduction allowable under Section 2055 of the Code and/or the marital deduction provided by Section 2056 for estate tax purposes in a situation where post-mortem administrative expense accumulations were paid from post-mortem accumulated income, and that no portion of these expenses were paid from the principal or corpus of the decedent's estate.

The Court of Appeals for the Fifth Circuit in the *Warren* case unequivocally held that the payment of post-mortem administrative expenses from accumulated estate income *does not reduce* either the amount of the allowable charitable deduction or marital deduction for federal estate tax purposes.

The decision of the Court of Appeals in this case is directly and absolutely contrary to the decision in *Warren*, wherein the Court of Appeals concluded that it was legally permissible for the Commissioner to reduce the amount of the estate's charitable deduction, otherwise allowed by Section 2055, by the amount of the post-mortem administrative accumulated expenses and associated interest, whether or not these expenses were paid from estate principal or accumulated income.

This is the basis and only basis for which we seek review by the Supreme Court of Petitioner's case and the Opinion of the Court of Appeals.

The comments that appear hereinafter in this Brief have been made to point up and bring into sharper focus the conflict between the two decisions and also the developing conflict between the recent decisions of the Tax Court of the United States and several other appellate cases involving this issue.

ARGUMENT

Petitioner in reply to the contentions contained in the Brief of Respondent in Opposition to the Petition, submits the following:

1. The Respondent at Paragraph 1, Page 6 of its Brief in Opposition alleges that administrative expenses are chargeable against the gross estate regardless of their source of payment, citing Section 2053(a) of the Code, that provides the general rules that states "the value of the taxable estate shall be determined by deducting from the value of the gross estate" the amount of funeral expenses, administrative expenses, claims against the estate and unpaid mortgages.

It is Petitioner's contention that this case does not directly involve Section 2053(a) of the Code but instead involves the proper construction of Section 2055, which provides for the deduction of all charitable bequests from the value of the decedent's gross estate, in order to determine the net estate, upon which the estate tax is levied.

Respondent also states that "Income received by an estate during its administration ('post-mortem income') is not included in the gross estate for estate tax purposes."

We quite agree with this observation and point out to the Court that there is absolutely no contention that the estate's post-mortem income should be includable in the decedent's gross estate, either directly or indirectly.

The sole issue raised in the Petition is whether or not there is a conflict between the Opinion of the Court of

Appeals and the Decision of the Fifth Circuit in *Estate of Dorothy J. Warren, Dec. v. Commissioner*, 981 F.2d 776 (5th Cir. 1993).

The conflict between these two decisions arises essentially as follows:

The Court of Appeals in this case held that the estate's charitable deduction, under Section 2055, must be reduced by the amount of the post-mortem accruing administrative expenses, whether or not they were paid from post-mortem income accumulations or the principal of the estate on hand at date of death.

The Fifth Circuit in *Warren* held directly to the contrary and respected a stipulation of the parties, pursuant to which 72 1/2% of the post-mortem administrative expenses were allocated to or paid from post-mortem income accumulations, and that by reason of this action, the Court held that the charitable deduction available to the estate was *not* reduced by the payment of administrative expenses from accumulated estate's income, as contended by the Commissioner.

We submit, therefore, that there is an irreconcilable conflict between the decision of the Court of Appeals and the decision of the Fifth Circuit in *Warren*.

On Page 7 of Respondent's Brief, there is a partial quotation from Senate Committee Report No. 1013, 80th Cong., 2d Sess. Pt. 2, at 6 (1948) wherein it is stated, " . . . *if the estate income is used to pay, claims so as to increase the residue,* such increase in the residue is acquired by purchase and not by bequest. Accordingly, the value of any such additional part of the residue passing to the surviving spouse cannot be included in the amount of the marital deduction."

We wish to point out to the Court that the above Committee Report refers only to "claims" against the estate and in no place mentions post-mortem accumulations of administrative expenses.

Later in this Brief, we will develop more fully the difference in estate tax treatment between claims against

the estate and post-mortem accumulated administrative expenses.

2. The Respondent in Paragraph 2, Page 8 of its Brief, contends that the Court of Appeals correctly rejected Petitioner's contention that the charitable deduction under Section 2055 should be based upon the actual distributions to the Foundation.

Petitioner has never contended that the amount of the charitable deduction allowable under Section 2055 should be increased by one cent of the estate's post-mortem income accumulations.

Petitioner agrees that the charitable deduction is geared to the value of the decedent's estate on hand at date of death, and that post-mortem income accumulations do not either increase or decrease the amount of the allowable deduction.

The point in the case is that since the controversial administrative expenses were shown to have been paid from post-mortem income accumulations, then there is no way that it can logically be said that the decedent's gross estate has been diminished by the payment of administrative expenses, and to the contrary, the charitable donee received from the principal of the decedent's estate on hand at date of death, an amount of property exactly equal in amount to the charitable deduction taken on the estate tax return under Section 2055.

The only purpose for which Petitioner tabulated the total payments made from the decedent's estate to the Foundation was to show that the charitable legatee received from the principal of the decedent's estate, an amount of property not less in value than the charitable deduction claimed under Section 2055. Additionally, the tabulation was made to show that the charitable donee received a great deal more in property than the amount of the charitable deduction claimed on the estate tax return (Form 706).

3. The Respondent at Paragraph 3, Page 8 of its Brief eludes to the fact that "The court of appeals did not

err in disregarding the unopposed Florida probate court order that allowed petitioner to pay administrative expenses from post-mortem income."

We submit that entirely too much emphasis is being placed by Respondent on the question of the source of the authority pursuant to which Petitioner's Personal Representatives admittedly paid certain post-mortem accumulated administrative expenses from post-mortem accumulated income. The point in the case is that the Personal Representatives did in fact pay the administrative expenses from post-mortem income and, therefore, none of these payments had the effect of reducing the amount of the decedent's gross or net taxable estate and, therefore, the amount of the charitable deduction should not be reduced, as determined by the Commissioner and affirmed by the Court of Appeals.

4. The Respondent in Paragraph 4, Page 9 of its Brief makes the positive statement that "The decision in this case does not conflict with *Estate of Warren v. Commissioner* . . . "

We urge the Court to reject this contention, since we earnestly feel that any fair objective reading of the Opinion of the Fifth Circuit in *Warren* makes it crystal clear that where a portion of the estate's post-mortem administrative expenses are paid from post-mortem income accumulations, the estate is not bound, as a matter of law, to reduce the amount of the marital or the charitable deduction otherwise allowable to the estate for federal estate tax purposes.

Admittedly, *Warren* arose under a different factual pattern than Petitioner's case, but the underlying legal principle, as it relates to the issue, we submit, is identical.

We urge the Court to grant this Petition, so that this conflict between the Court of Appeals and the Fifth Circuit can be resolved, once and for all.

5. Respondent, at Page 11 of its Brief cites the case of *Estate of Gordon P. Street v. Commissioner*, 974 F.2d 723 (6th Cir. 1992).

The Sixth Circuit reversed the Tax Court and " . . . held that the marital deduction is reduced by administrative expenses paid from either principal or income, . . . " but at the same time, interestingly enough, the Court went on to hold that post-mortem interest accumulations do not reduce the amount of the marital deduction or, for that matter, the charitable deduction.

Respondent states "Interest expense is treated differently because it accrues after death; estate income used to pay that expense therefore would not affect the size of the gross estate."

To further point out the absurdity of the Respondent's position in this case, the uncontradicted facts show that all of the administrative expenses, just as interest expense in the *Street* case, arose and were accumulated after the decedent's death and did not constitute any type of claim against the decedent's estate at time of death and, that all of the administrative expenses involved in this case were paid from the estate's accumulated income and, therefore, again do not affect the size of the decedent's gross estate.

We, therefore, contend that the payment of post-mortem administrative expenses, just as post-mortem interest expense in *Street*, does not affect the size of the decedent's gross estate and hence, these payments do not reduce the amount of the charitable deduction allowable to the estate under Section 2055.

6. Since the filing of the Petition in this case, the Tax Court of the United States has rendered two very significant decisions involving the issue directly involved in this case and should, we think, be properly brought to the attention of the Court.

The first of these cases is *Estate of Otis C. Hubert, Dec. v. Commissioner*, T.C. Docket No. 22333-90, 101 T.C. No. 22, filed October 19, 1993.

The Tax Court in *Hubert* held that an estate was not required to reduce its marital and charitable deductions by the amount of estate administrative expenses paid out

of estate income. In so holding, the Tax Court expressly declined to follow the decision of the Court of Appeals in *Street* and also expressly declined to follow the decision of the Court of Appeals in this case.

Contrary to the Court's decision in *Street*, the Tax Court in *Hubert* concluded that Treasury Regulation Section 20.2056(b)-4(a) did not mandate a set-off against the marital deduction for administrative expenses allocated to income. According to the Tax Court, that Regulation is merely a valuation provision that requires material limitations on the right to receive income to be taken into account when valuing the property interest passing to a surviving spouse.

Moreover, the Court noted that the Legislative history of Section 20.2056, which indicates that *"claims against the estate would reduce a marital deduction but was not applicable to administrative expenses"*.

According to the Tax Court, there is a clear distinction between claims against an estate, which are in existence at the date of the decedent's death and relate to corpus, and administrative expenses, which come into existence only after the date of the decedent's death and can logically be charged either to income or corpus.

Therefore, we find that the Tax Court, a trial court of nationwide jurisdiction, has expressly refused to follow the decision in *Street* and also has refused to follow the decision in this case, rendered by the Court of Appeals, as it relates to the issue directly involved.

Petitioner has attached as Appendix "A" all of the Opinion of the Tax Court in the *Hubert* case, except that the two dissenting and concurring opinions have been intentionally omitted. As the Court will see from Appendix "A", the *Hubert* case was reviewed by the full Tax Court and two of the judges filed dissenting and concurring opinions.

The Tax Court in *Hubert*, in expressly declining to apply the decision of the Court of Appeals in this case

and the decision of the Sixth Circuit in *Street*, stated (Appendix A, *infra* p. 22a):

> Thus, the Court of Appeals concluded that payment of administration expenses from income of the estate should reduce the marital deduction, but payment of interest on estate and inheritance taxes from income should not reduce the marital deduction. See also *Burke v. United States* [93-1 USTC Section 60,132], 994 F.2d 1576 (Fed. Cir. 1993), and *Fisher v. United States*, 28 Fed. Cl. 88 (1993), which rely on the rationale of *Estate of Street* with respect to administration expenses.
>
> Respectfully, we disagree with the reasoning of the Court of Appeals and decline to follow its decision in *Estate of Street*.

Both the dissenting and concurring opinions of Judge C. J. Hamblen and Judge J. Halpern in *Hubert* cited and commented briefly on the Court of Appeals Opinion in this case.

The Tax Court rendered a second Opinion involving this issue in *Estate of Frances Blow Allen v. Commissioner*, T.C. Docket No. 309-91, 101 T.C. No. 23, filed October 20, 1993. The Tax Court, in *Allen*, held that the marital trust there involved should not be reduced by the amount of administrative expenses paid from other sources and expressly declined to follow the decision of the Sixth Circuit in *Street*.

Petitioner has attached as Appendix "B" Commerce Clearinghouse's Digest, *Federal Estate and Gift Tax Reports*, Number 226, dated October 26, 1993, reporting of the Decision of the Tax Court in *Allen*.

Counsel for Petitioner is fully aware that the Supreme Court does not ordinarily resolve conflicts between Federal Trial Courts and the various Courts of Appeal.

We have cited both the *Hubert* and *Allen* cases to simply show to the Court the continual litigation of the issue involved in this case and what we think is the practical necessity of the Court's granting this Petition, so

as to resolve the conflict between the decision of the Court of Appeals and the decision of the Fifth Circuit in *Warren*.

CONCLUSION

Petitioner respectfully suggests to the Court that the Petition filed in this case should be granted, so that the direct conflict between the Opinion of the Court of Appeals and the Opinion of the Fifth Circuit in *Warren* can be resolved, once and for all, in order to resolve a point of federal estate taxation, which has been a recurring one over a period of many years.

Because of the continuous and regularity with which the issue involved in this case is and has been litigated, we are somewhat puzzled, as to why Respondent has elected not to agree to the Court's granting the Petition, in order to resolve the conflict and the multiplicity of cases that have arisen involving this issue and which continue to be litigated, even to the present time.

We therefore urge the Court to grant the Petition.

Respectfully submitted,

WILLIAM R. FRAZIER
Counsel of Record
FRAZIER & FRAZIER
Attorneys for Petitioner
1515 Riverside Avenue
Suite A
Jacksonville, FL 32204
(904) 353-5616

Dated November 22, 1993

"APPENDIX A"

[CCH Dec. 49,342] Estate of Otis C. Hubert, Deceased, C&S/Sovran Trust Company (Georgia), N.A., A National Banking Association, Co-Executor, v. Commissioner.

Docket No. 22333-90. 101 TC ___, No. 22. Filed October 19, 1993. [Appealable, barring stipulation to the contrary, to CA-11. – CCH.]

[*Code Secs. 642, 2055 and 2056*]

[Estate tax: Marital and charitable deductions: Property passing to surviving spouse and charity: Settlement agreement.] Pursuant to a good faith settlement of a will contest alleging undue influence, decedent's 1982 will and codicils thereto were amended to provide, inter alia, for the division of the residuary estate into marital and charitable portions with the allocation of principal, accumulated income, and expenses to each.

Held: The amounts passing to the marital and charitable shares are those in the settlement agreement and are not limited to the amounts which would have passed under the 1982 will and codicils.

Held, further, the marital and charitable deductions are to be reduced only by the portion of administration expenses allocated to principal and not by amounts allocated to income. *Estate of Street v. Commissioner* [92-2 USTC ¶ 60,112], 974 F.2d 723 (6th Cir. 1992), affg. in part, revg. in part and remanding [Dec. 45,201(M)] T.C. Memo. 1988-553, not followed.

Held, further, the marital and charitable portions are not to be reduced by imputed income at the rate of 7 percent per annum; the marital and charitable deductions are valued at the date of death and only appropriate charges to principal will reduce the deduction.

David W. Aughtry, and James M. McCarten, 233 Peachtree St., N.E., Atlanta, Ga., for the petitioner. Willard N. Timm, Jr., for the respondent.

Opinion

CLAPP, Judge: Respondent determined a deficiency in petitioner's estate tax in the amount of $14,052,146. After concession by the parties, the remaining issues for decision are: (1) Whether the amounts of petitioner's marital and charitable deductions are limited to the amounts passing to the marital and charitable shares under the 1982 will and three codicils, or are the amounts actually passing under a settlement agreement to the marital and charitable shares as reduced by obligations charged to the respective shares; (2) whether the amounts of the marital and charitable deductions must be reduced by administration expenses paid from the marital and charitable portions[1] under the settlement agreement, without regard

---

[1] We are using the terms "marital portion" and "charitable portion" to mean the amounts received by the spouse and the charity, respectively, under the settlement agreement. Pursuant to the settlement agreement, the marital and charitable portions include income accumulated to the date of distribution. The terms "marital portion" and "charitable portion" should not be confused with the terms "marital share" and "charitable share" or "marital deduction" and "charitable deduction".

to whether the estate allocated those expenses to income; and (3) whether the marital and charitable portions must be discounted by 7 percent per annum to take into account income deemed to be earned by the residue.[2]

This case was submitted fully stipulated under Rule 122. We incorporate by reference the stipulation of facts and attached exhibits. All section references are to the Internal Revenue Code as in effect at the date of decedent's death, and all Rule references are to the Tax Court Rules of Practice and Procedure.

Petitioner is the Estate of Otis C. Hubert (decedent). Decedent was a resident of Marietta, Georgia, when he died on June 2, 1986. C&S/Sovran Trust Company (C&S) is the coexecutor of decedent's estate. On the date the petition was filed, C&S had its principal place of business in Atlanta, Georgia.

At the time of his death, decedent was married to Ruth S. Hubert (Mrs. Hubert). The Huberts had four children: Richard N. Hubert, Marilyn Hubert Kemper, Judith Hubert Manning, and Deborah Hubert Jones.

In January 1982, decedent executed the last will to be signed prior to his death (the 1982 will). That will superseded his previous will, which had been executed in 1977.

---

[2] The Court has severed, for decision in a separate opinion, *Estate of Hubert v. Commissioner* [Dec. 49,345(M)] T.C. Memo. 1993-482, the issue of whether bequests in the amount of $100,000 each to two subtrusts providing for the support of the missionary work of charitable organization through two named individuals and for the establishment of foreign mission field medical clinics qualify for a charitable deduction.

The 1982 will was modified three times by codicils executed between February 4, 1982, and June 8, 1983. Decedent's nephew, Robert H. Owen (Owen), drafted the will and the three codicils.

In addition to certain specific bequests, the 1977 will left, in trust, an amount equal to the maximum marital deduction; however, if the estate tax due from the estate (before application of any credits) were less than any credits available to the estate, the marital bequest was to be reduced to that amount which would cause the estate tax owed by decedent's estate (before application of any credits) to equal the total of all credits finally allowed. Decedent's intent was to fully utilize all credits and deductions. The income from the trust was payable to Mrs. Hubert for her life, with the remainder to charity. Mrs. Hubert had a general power of appointment over the trust. The 1977 will also established a charitable remainder unitrust from the residue of the estate. The trustee had the discretion to distribute 5 percent of the net assets of the charitable trust annually to Mrs. Hubert or any of the Hubert children. Upon the death of Mrs. Hubert, the charitable trust terminated, and the remainder was to be distributed outright to charity.

The 1982 will left the residue of decedent's estate in trust, the income of which was to be paid to Mrs. Hubert, with the remainder to charity. Mrs. Hubert had a general power of appointment. The second codicil to the 1982 will eliminated Mrs. Hubert's general power of appointment.

Upon decedent's death, will contests were filed by various members of the Hubert family, including Mrs. Hubert. The will contest instituted by Mrs. Hubert

requested the Probate Court to strike the second codicil to the 1982 will or, in the alternative, to strike the 1982 will and all the codicils, because of alleged undue influence by Owen in favor of the charitable remainder beneficiaries. In June 1987, the Hubert family, Owen, and the district attorney for Cobb County, Georgia, where the will was being probated, entered into an "Agreement of Interested Parties" (the first agreement), which purported to resolve all of the differences among the competing interests under the will.

The Georgia revenue commissioner challenged the first agreement alleging that he was a necessary party to ensure that the charitable beneficiaries were treated fairly. As a result of negotiations, which included the Georgia revenue commissioner and the Georgia attorney general as representatives for the charities, the first agreement was supplanted by the "Second and Final Settlement Agreement" (settlement agreement) on October 10, 1990, which was approved by the Superior Court of Cobb County in an Order, Judgment, and Decree. The Cobb County Probate Court entered a final order adopting the Order, Judgment, and Decree as binding in its proceedings on November 28, 1990.

The settlement agreement amended the 1982 will and codicils by deleting item VIII, which disposed of the residuary estate, and all codicil provisions related to that item. In lieu thereof, the settlement agreement added various provisions, including provisions for the division of the residuary estate between the marital and charitable portions and for the allocation of expenses between the marital and charitable portions. Under the settlement agreement, Mrs. Hubert was named beneficiary of a part

of the residue in two trusts: The marital trust, over which she had a general power of appointment, and the QTIP trust. The charity received the rest of the residue outright.

Based on the first agreement, an estate tax return, Form 706, was filed on September 2, 1987. Respondent issued a notice of deficiency on August 31, 1990, disallowing $12,650,592 of the marital deduction and $12,502,655 of the charitable deduction, as well as making adjustments to the deduction for debts of the decedent and to the amount of adjusted taxable bequests.

Limitations on Deductions Based on the 1982 Will and Codicils

The first issue for decision is whether the marital and charitable deductions are limited by the amounts Mrs. Hubert and the charity would have taken under the 1982 will and codicils.

Marital Deduction

Section 2056(a) provides in pertinent part:

> For purposes of the tax imposed by section 2001, the value of the taxable estate shall . . . be determined by deducting from the value of the gross estate an amount equal to the value of any interest in property which passes or has passed from the decedent to his surviving spouse, but only to the extent that such interest is included in determining the value of the gross estate.

In defining whether an interest in property has "passed from the decedent to his surviving spouse" in the context

of a will contest, section 20.2056(e)-2(d)(2), Estate Tax Regs., states:

> If as a result of the controversy involving the decedent's will, or involving any bequest or devise thereunder, a property interest is assigned or surrendered to the surviving spouse, the interest so acquired will be regarded as having "passed from the decedent to his surviving spouse" only if the assignment or surrender was a bona fide recognition of enforceable rights of the surviving spouse in the decedent's estate. Such a bona fide recognition will be presumed where the assignment or surrender was pursuant to a decision of a local court upon the merits in an adversary proceeding following a genuine and active contest. However, such a decree will be accepted only to the extent that the court passed upon the facts upon which deductibility of the property interests depends. If the assignment or surrender was pursuant to a decree rendered by consent, or pursuant to an agreement not to contest the will or not to probate the will, it will not necessarily be accepted as a bona fide evaluation of the rights of the spouse.

Respondent argues that petitioner's marital deduction is limited to the lesser of the amount distributed to Mrs. Hubert under the settlement agreement or the amount that would have been so distributed under the 1982 will and codicils. Presumably, respondent's contention is that Mrs. Hubert did not have an enforceable right in decedent's estate to any amount in excess of what she would have received under the 1982 will and codicils.

Petitioner argues that "(i) a good faith compromise of (ii) a *bona fide* will dispute, (iii) involving uncontested provisions of state law, is absolutely dispositive of the question of enforceable rights." Petitioner contends that, although a settlement agreement cannot definitively determine questions of law, it can conclusively resolve questions of fact. Petitioner concludes that, since the State law in this case is clear and the dispute is inherently factual, the settlement agreement should control.

In deciding whether a settlement agreement is a "bona fide recognition of enforceable rights of the surviving spouse in decedent's estate", this Court has looked to whether the agreement was made in good faith as the result of arm's-length negotiations. *Estate of Barrett v. Commissioner* [Dec. 20,406], 22 T.C. 606, 611 (1954).

However, in *Commissioner v. Estate of Bosch* [67-2 USTC ¶ 12,472], 387 U.S. 456 (1967), the Supreme Court held that a Federal court deciding the estate tax consequences of an attempted disclaimer was not bound by the State trial court's adjudication of the property rights involved. Citing *Erie R. Co. v. Tompkins*, 304 U.S. 64 (1938), the Court noted that "state law as announced by the highest court of the State is to be followed." *Commissioner v. Estate of Bosch, supra* at 465. Moreover, the Court explained that the State's intermediate appellate court decisions should be considered in deciding State law unless the Federal court is convinced that the highest court of the State would rule otherwise. Therefore, the Court concluded that a Federal court may not always be bound by the decision of the intermediate appellate court and that "when the application of a federal statute is involved, the decision of a state trial court as to an

underlying issue of state law should a fortiori not be controlling." *Id.* Finally, the Court explained:

> the underlying substantive rule involved is based on state law and the State's highest court is the best authority on its own law. If there be no decision by that court then federal authorities must apply what they find to be the state law after giving *"proper regard"* to relevant rulings of other courts of the State. In this respect, it may be said to be, in effect, sitting as a state court. [*Id.*; emphasis added; citation omitted.]

In light of the Supreme Court's decision in *Estate of Bosch*, courts have concluded that if the decision of a State trial court on a matter of State law is not binding for estate tax purposes, a good faith settlement of such an issue cannot be either. *Ahmanson Found. v. United States* [81-2 USTC ¶ 13,438], 674 F.2d 761, 774 (9th Cir. 1981). We agree. In deciding whether the surviving spouse has enforceable rights in decedent's estate, courts must look behind any settlement agreement to ensure that the claim on which it is based is valid. *Estate of Brandon v. Commissioner* [87-2 USTC ¶ 13,733], 828 F.2d 493, 499 (8th Cir. 1987), revg. and remanding [Dec. 42,911] 86 T.C. 327 (1986).

While we agree that we are not bound by the settlement agreement for our decision of Mrs. Hubert's enforceable rights, we conclude that the agreement should not be ignored here. We have looked at the adversarial or nonadversarial nature of the proceedings in the State courts to determine the weight to be given such settlement agreements. See *Estate of Sawyer v. Commissioner* [Dec. 36,371], 73 T.C. 1 (1979) (Tax Court followed the

decision of the Court of Appeals of Ohio because the decision was the result of a bona fide adversary proceeding, and the Court could not conclude that the Supreme Court of Ohio would not follow the lower court decision); *Harrah v. Commissioner* [Dec. 35,358], 70 T.C. 735, 754 (1978) (Tax Court followed the characterization of property in a settlement agreement approved by a Nevada divorce court because the Court believed "the Nevada Supreme Court would have approved the action taken by the divorce court had it been called upon to review it", emphasizing the adversarial nature of the settlement); *Estate of Rowan v. Commissioner* [Dec. 30,025], 54 T.C. 633 (1970) (Tax Court disregarded the determination of property ownership made by the Superior Court of California where it was not the result of bona fide adversary litigation and made an independent determination of the facts and law).

The parties have stipulated that the settlement agreement was the result of a bona fide adversary proceeding. Under the settlement agreement, Mrs. Hubert received in value more than half of what she would have received if she had succeeded in having the second codicil declared invalid as the product of undue influence and substantially all of what she would have received if she had succeeded in having the 1982 will and codicils declared invalid as the products of undue influence. Moreover, this was a settlement among adverse parties with significant interests to protect in the litigation, including the Georgia attorney general and the Georgia revenue commissioner, whose right to participate in the litigation was litigated all the way to the Supreme Court of Georgia. The settlement agreement also was approved by the

Superior Court of Cobb County. Under Georgia law a settlement agreement sustaining a will challenge can be approved by the Superior Court only "after a hearing, notice of which shall be given as the court shall direct, at which evidence is introduced and at which the judge finds as a matter of fact that the caveat is meritorious." Ga. Code Ann. sec. 53-3-22(a) (Michie 1982).

In addition, this is not a circumstance in which respondent's interests were hurt by the compromise reached by the parties. If the probate of the estate had proceeded without challenge, and the estate tax return had been filed based on the 1982 will and codicils, Mrs. Hubert would have been entitled to an income interest for life, payable at least annually, in the entire residue of the estate. Therefore, petitioner could have made a QTIP election and been entitled to a deduction for the entire residue. We note that respondent has conceded that the second settlement agreement modified the 1982 will and codicil so that section 2056(b)(7)(B)(i)(III) does not bar the marital deduction. Since the estate would have been entitled to a full deduction for the residue under the 1982 will and codicils, there is no way that the parties could have acted in a manner contrary to respondent's interests.[3]

---

[3] We note that the additional tax that would arise if respondent prevailed on this argument is the result of the inconsistent treatment given to settlement agreements in the regulations. If Mrs. Hubert did not have an enforceable right to all of what she received under the settlement agreement, petitioner would be entitled to deduct only the amount she would have received under the 1982 will and codicils. The rationale for the result is that any amount to which she did not have an enforceable right did not pass to her from decedent, but was given to her by the

Taking all of the circumstances surrounding the settlement agreement into consideration, we are convinced that what Mrs. Hubert received under the settlement agreement is in satisfaction of enforceable rights in decedent's estate. Although the regulations state that the settlement agreement will not *necessarily* be accepted as a bona fide evaluation of such rights, they do not require rejection of such settlement agreement. In this instance we think it is appropriate to recognize the amounts passing to Mrs. Hubert under the settlement agreement as passing from decedent, especially in the absence of any suggestion that the settlement agreement was entered into for post mortem tax planning purposes.

Therefore, we hold that the marital deduction is not limited by the amount Mrs. Hubert would have taken under the 1982 will as amended by the second codicil.

Charitable Deduction

Respondent argues that the charitable deduction also is limited to the lesser of the amount the charity would have received under the 1982 will and codicils or the

---

charity in exchange for dropping her challenge. However, under the regulations, petitioner is not entitled to a charitable deduction for the amount the charity gave up in the settlement, presumably because if the charity never actually received the property before giving it up, it was not a bequest, legacy, devise, or transfer to or for the use of a charitable organization. Consequently, if Mrs. Hubert did not have an enforceable right to all of the amount she received under the settlement, a portion of the residue which was left entirely to either Mrs. Hubert or the charity would be treated as having passed to neither of them.

amount it actually received under the settlement agreement. Petitioner argues that the charitable deduction is equal to the amount the charity actually received provided the settlement was not collusive. We note that the parties appropriately agree that "the Second Settlement Agreement modified the 1982 Will and three Codicils so that the split interest provisions under I.R.C. section 2055(e) [do] not bar a deduction for the charitable gift". See *Flanagan v. United States* [87-1 USTC ¶ 13,718], 810 F.2d 930 (10th Cir. 1987); *First Natl. Bank v. United States* [84-1 USTC ¶ 13,558], 727 F.2d 741 (8th Cir. 1984); *Estate of Strock v. United States* [87-1 USTC ¶ 13,717], 655 F. Supp. 1334 (W.D. Pa. 1987); *Northern Trust Co. v. United States*, 41 AFTR 2d 78-1523, 78-1 USTC ¶ 13,229 (N.D. Ill. 1977); Rev. Rul. 89-31, 1989-1 C.B. 277. Therefore, the parties agree that petitioner is entitled to some amount of charitable deduction. Moreover, since the charity will receive less under the settlement agreement than it would have received under the will, respondent and petitioner are in agreement that the settlement agreement controls the amount of the charitable deduction.

Allocation of Expenses

The second issue for decision is whether the marital and charitable deductions must be reduced by expenses allocated to income of the estate.

The 1982 will gave the executors of decedent's estate the power "to charge any expenses against income or principal or apportion the same". The executors allocated $506,989 as funeral and administration expenses to the

principal of the estate. All other administration expenses were allocated to income.

Respondent argues that the amount of a marital or charitable deduction must be reduced by the entire amount of administration expenses, whether those expenses are allocated to principal or to income. Respondent cites section 20.2056(b)-4(a), Estate Tax Regs., and the legislative history of section 2056 as support for the proposition. In addition, respondent argues that the courts have "uniformly recognized" that administration expenses reduce the marital and charitable deductions regardless of whether those expenses are paid out of income or principal. Respondent contends that both Georgia law and the language of the settlement agreement also mandate such a result. We disagree.

Before considering this issue in detail, it is helpful to consider an overview of the operation of estate accounting and estate taxes. The starting point for determining Federal estate taxes is the date-of-death (or alternate valuation date) value of the property of the estate. Deductions are allowed for various expenses of the estate, as well as for claims against the estate and bequests to the decedent's spouse and to charity. Income earned by the estate has no effect on the estate for Federal estate tax purposes. It is accounted for separately in the estate's probate account and is taxed separately on the estate's Forms 1041.

Executors have been granted significant flexibility in accounting for the estate's administration expenses, both for estate and income tax purposes, and for probate accounting purposes. Congress has granted the executor

the option of deducting administration expenses on either the estate return, Form 706, or the fiduciary income tax return, Form 1041. Sec. 642(g). In addition, many States give the decedent the option of authorizing the executor to allocate such expenses to principal or to income at the executor's discretion. If the administration expenses were paid out of principal, they would reduce the amount of such principal received by the beneficiaries and would reduce the marital and charitable deductions. However, we conclude that the administration expenses that are allocable to income in this case do not change the amount of the estate principal received by the spouse or the charity and do not reduce the marital and charitable deductions. Administration expenses are incurred and accrue during administration and should not be confused with claims against the estate which existed and accrued at the date of death.

Our conclusion that the marital and charitable deductions are not reduced by payment of administration expenses allocated to income does not lead to a double deduction in violation of section 642(g). Section 642(g) prohibits a deduction under section 2053 or 2054 for any administration expenses deducted on the estate's income tax return. However, section 642(g) does not prohibit or reduce deductions under section 2055 or 2056. The deductions under sections 2055 and 2056 are based on the date-of-death value of the property received by the charity and the spouse from the gross estate. The executor's ability to preserve the value of the marital and charitable bequests by allocating administration expenses to income is in no way barred by section 642(g).

The allocation of the expenses in the case before us is governed by Georgia law. Georgia law authorizes allocation of expenses to income rather than principal, if provided in the will. Ga. Code Ann. secs. 53-2-101, 53-15-3 (Michie 1982). The 1982 will authorized such an allocation, and this provision was not affected by the settlement agreement. To the extent the executor exercised its discretion and allocated administration expenses to income, the marital and charitable deductions are not reduced by payment of those expenses.

Respondent argues that section 20.2056(b)-4(a), Estate Tax Regs., controls this question. That section states, in relevant part:

> Marital deduction; valuation of interest passing to surviving spouse. – (a) *In general.* * * * The marital deduction may be taken only with respect to the net value of any deductible interest which passed from the decedent to his surviving spouse, the same principles being applicable as if the amount of a gift to the spouse were being determined. *In determining the value of the interest in property passing to the spouse* account must be taken of the effect of any material limitations upon her right to income from the property. An example of a case in which this rule may be applied is a bequest of property in trust for the benefit of the decedent's spouse but the income from the property from the date of the decedent's death until distribution of the property to the trustee is to be used to pay expenses incurred in the administration of the estate. [Emphasis added.]

We do not interpret section 20.2056(b)-4(a), Estate Tax Regs., as mandating a setoff against the marital deduction

for administration expenses allocable to income. That section is merely a valuation provision which requires material limitations on the right to receive income to be taken into account when valuing the property interest passing to the surviving spouse. The fact that income from property is to be used to pay expenses during the administration of the estate is not necessarily a material limitation on the right to receive income that would have a significant effect on the date-of-death value of the property of the estate.

On the facts before us, we find that the trustee's discretion to pay administration expenses out of income is not a material limitation on the right to receive income. Under section 2056(b)(4) and section 20.2056(b)-4(a), Estate Tax Regs., the value of the interest passing to the spouse and the effect of any encumbrance on that interest shall be determined "as if the amount of a gift to the spouse were being determined." Therefore, we look to the gift tax provisions and consider how they treat the payment of expenses out of the income of a trust that was given to a spouse. Under section 2523(e), in order for a donor to be entitled to a deduction for a gift in trust to his spouse over which the spouse has a general power of appointment, the spouse must be entitled to all of the income from the trust. Under section 25.2523(e)-1(f)(3), Gift Tax Regs., a spouse is considered to receive all of the income from a trust even if "trustees' commissions, and other charges" are paid out of income, provided the spouse is not deprived of substantial beneficial enjoyment. That section is similar to section 20.2056(b)-(5)(f)(3). Estate Tax Regs. In interpreting those sections, respondent has considered the effect of a power

"To charge to income or principal, executor's or trustee's commissions, legal and accounting fees, custodian fees, and similar administration expenses" on the marital deduction. Respondent concluded that such a power "does not result in the disallowance or *diminution* of the marital deduction." Rev. Rul. 69-56, 1969-1 C.B. 224 (emphasis added). While we recognize that the revenue ruling is not binding precedent, it does present respondent's position on this subject. *Crow v. Commissioner* [Dec. 42,339], 85 T.C. 376, 389 (1985).

In the case before us, the power is essentially the same as the power in the revenue ruling. Moreover, the income used to pay administration expenses is insubstantial compared to the lifetime of income Mrs. Hubert will receive from the property. Therefore, she is not deprived of substantial beneficial enjoyment, and she would be treated, under section 25.2523(e)-1(f)(3), Gift Tax Regs., as having received all of the income from the trust. If Mrs. Hubert is treated as having received all of the income from the trust, there can be no material limitation on her right to receive income.

We also reject respondent's interpretation of the legislative history of the marital deduction, which states that *claims* against the estate paid out of income increase the residue by purchase, not bequest, and therefore "the value of any such additional part of the residue passing to the surviving spouse can not be included in the amount of the marital deduction." S. Rept. 1013 (Part II), 80th Cong., 2d Sess. (1948), 1948-1 C.B. 331, 335. The Senate report describes the result only if income is used

to pay *claims against the estate;* it does not discuss administration expenses at any point. There is a clear distinction between claims against the estate and administration expenses which are allocable to income, and this distinction mandates different treatment of the two. Claims against the estate are, by definition, in existence at the date of death; therefore, by their very nature, claims against the estate relate to corpus and must be charged thereto. By contrast, administration expenses come into existence only after the death of the decedent and may relate to both income and corpus. As a result, administration expenses logically can be charged to either income or corpus. Here they were charged to income in accordance with the will and Georgia law. Accordingly, the legislative history cited by respondent does not control the treatment of administration expenses in the case before us.

This Court has spoken on this issue in *Estate of Richardson v. Commissioner* [Dec. 44,388], 89 T.C. 1193 (1987), and *Estate of Street v. Commissioner* [Dec. 45,201(M)], T.C. Memo. 1988-553, affd. in part and revd. in part [92-2 USTC ¶ 60,112], 974 F.2d 723 (6th Cir. 1992). In *Estate of Richardson,* the decedent left to his wife the amount of his residuary estate necessary to maximize all of his estate tax deductions in order to make his estate nontaxable for Federal estate tax purposes. The decedent's executors were given the power to allocate expenses between income and principal. Respondent argued that the marital deduction should be reduced by the amount of interest payable on the estate's Federal estate taxes and State inheritance taxes, even though the executors had allocated the interest to income.

We concluded: "Whether an expenditure on behalf of an estate is chargeable to principal, or the income produced thereby, depends on the law of the State wherein decedent was a resident at the time of his death, or upon the terms of decedent's will." *Estate of Richardson v. Commissioner, supra* at 1201. In that case, there were no provisions of State law dictating where the interest should be charged. Therefore, we looked to the language of the will and determined that, based on the decedent's intent to minimize taxes, the executors had the power to charge the interest against income and, thereby, not reduce the marital deduction.

In *Estate of Street*, on similar facts we held that Tennessee law permitted a decedent to grant the power to allocate administration expenses between income and principal. We held that the marital deduction was not reduced by the amount of the expenses allocated to income.

We note that the fact that the marital bequest in *Estate of Street* was in trust did not affect our reasoning in that case. Respondent argues that the fact of the trust should make a difference, because if Mrs. Hubert is receiving only an income interest and part of the income is used to pay expenses, the value of the interest passing to Mrs. Hubert is reduced. However, respondent ignores the fact that, because Mrs. Hubert has a general power of appointment over one of the trusts and the other trust is a qualified terminable interest trust, Mrs. Hubert is treated as having received the entire value of both trusts, not just the income portions.

On appeal, the Court of Appeals for the Sixth Circuit reversed our holding in *Estate of Street* with regard to administration expenses, concluding that payment of such expenses reduces the marital deduction whether the payment is allocated to income or to principal. However, the court upheld our holding that the payment of interest on estate taxes and inheritance taxes allocated to income does not reduce the marital deduction. *Estate of Street v. Commissioner* [92-2 USTC ¶ 60,112], 974 F.2d 723 (6th Cir. 1992), affg. in part, revg. in part and remanding.[4]

On the issue of the administration expenses, the Court of Appeals determined that section 20.2056(b)-4(a), Estate Tax Regs., was controlling. The Court of Appeals concluded that the regulation mandates a setoff against the marital deduction for administration expenses paid from income. The court reasoned:

> Income earned by the estate during * * * [the administration] period builds up the marital share. Expenses paid from income during this period have the effect of decreasing the amount of estate property distributable to the spouse. Therefore, the payment of administrative expenses from income must operate to reduce the size of the marital deduction, otherwise the spouse would receive a deduction which

---

[4] Respondent has now accepted the holding that the payment of interest on estate and inheritance taxes allocated to income does not reduce the marital deduction. Rev. Rul. 93-48, 1993-25 I.R.B. 9. Respondent has specifically limited her change in position to payments of interest and has reaffirmed her position regarding all other administration expenses. As we explain below, we see no valid distinction between interest and other administration expenses.

> exceeded the amount which was actually in the estate, and available for distribution. * * * [*Id.* at 727.]

The court found support for this reasoning in the legislative history of the marital deduction.

The Court of Appeals distinguished administration expenses from interest on estate and inheritance taxes on two grounds. First, citing *Estate of Richardson*, the court stated that the interest on taxes accrues after death, whereas administration expenses "accrue at death." As a result, the court determined that payment of interest on taxes from estate income does not affect the principal of the estate as it existed at the time of decedent's death, but payment of administration expenses from such income "will serve to build up the gross estate." *Id.* at 727. Second, the court noted that section 20.2056(b)-4(a), Estate Tax Regs., specifically mentions administration expenses in its example, but it does not mention interest on taxes. Therefore, the court held that the regulation was inapplicable to interest on taxes. *Id.* at 729. Thus, the Court of Appeals concluded that payment of administration expenses from income of the estate should reduce the marital deduction, but payment of interest on estate and inheritance taxes from income should not reduce the marital deduction. See also *Burke v. United States* [93-1 USTC ¶ 60,132], 994 F.2d 1576 (Fed. Cir. 1993), and *Fisher v. United States*, 28 Fed. Cl. 88, (1993), which rely on the rationale of *Estate of Street* with respect to administration expenses.

Respectfully, we disagree with the reasoning of the Court of Appeals and decline to follow its decision in *Estate of Street*. As stated above, we interpret section

20.2056(b)-4(a), Estate Tax Regs., to be a valuation provision. Therefore, unlike the Court of Appeals, we find that the regulation does not control the case before us. In addition, as noted previously, we conclude that the legislative history of the marital deduction does not mandate a different conclusion.

Moreover, we take issue with the Court of Appeals' analysis of the effect of income and expenses on the marital share. The court stated that income earned on estate property increases the marital share, and presumably the marital deduction, leading to a deduction greater than the amount distributed if payment of expenses from income does not reduce the marital deduction. However, income earned on estate property is not included in the gross estate. *Alston v. United States* [65-2 USTC ¶ 12,339], 349 F.2d 87 (5th Cir. 1965). As a result, under section 2056(a), such income does not lead to an increase in the amount of the marital deduction requiring a corresponding decrease for payment of administration expenses chargeable against income of the estate.

Finally, we disagree with the Court of Appeals' distinction between interest on estate and inheritance taxes and administration expenses. The fact that section 20.2056(b)-4(a), Estate Tax Regs., explicitly refers to administration expenses but does not mention interest on taxes is not relevant because the reference to administration expenses is "*An* example of a case in which this rule *may* be applied". Sec. 20.2056(b)-4(a), Estate Tax Regs. (emphasis added). Application of the regulation, when appropriate, is clearly not limited to administration expenses. Regardless of the regulation's treatment of

administration expenses and interest on taxes, it does not provide a useful distinction between the two.

In addition, administration expenses and interest on taxes cannot be distinguished according to the time at which they accrue. Both accrue after the date of death. Administration expenses, by their very nature, are incurred over the entire period of the estate's administration and can vary significantly from estate to estate. As a result, administration expenses are too uncertain at the date of death to accrue at that time. Our analysis in *Estate of Richardson v. Commissioner* [Dec. 44,388], 89 T.C. 1193 (1987), therefore applies to administration expenses as well as to interest on taxes, and we will follow our holding in that case.

Both respondent and the Court of Appeals cite *Estate of Roney v. Commissioner* [Dec. 24,026], 33 T.C. 801, (1960), affd. [61-2 USTC ¶ 12,040], 294 F.2d 774 (5th Cir. 1961), as support for their positions. In *Estate of Roney,* the decedent left the residue of his estate to his wife. The will made no provision as to the source for payment of administration expenses. The executor deducted the administration expenses on the estate's fiduciary income tax returns and did not reduce the marital deduction on the estate tax return by the amount of those expenses. In that case, we looked to Florida law and determined that the executor was required to pay administration expenses out of the residuary estate. Since the residuary estate does not include income, we determined that the marital deduction should be reduced by the amount of the expenses because the amount of principal received by the spouse was reduced to that extent.

The holding in *Estate of Roney* is not inconsistent with the result we reach in the case before us. We merely held in *Estate of Roney* that when administration expenses are required to be allocated to principal, the marital deductions is reduced by the amount of those expenses. Whether the deduction for the administration expenses is taken on Form 706 or Form 1041 is immaterial and irrelevant. See also *Alston v. United States, supra.*

Although *Estate of Wycoff v. Commissioner* [Dec. 31,831], 59 T.C. 617 (1973), aff'd. [74-2 USTC ¶ 13,037], 506 F.2d 1144 (10th Cir. 1974), was not cited by either party, we find it appropriate to discuss that case here. In *Estate of Wycoff,* the decedent's will provided:

> all inheritance, estate and transfer taxes due by reason of my death shall be paid out of that portion of my estate which is not included in the Marital Trust to be administered by my Trustee, unless, in the best business judgment and sole discretion of my executor, such taxes could be more prudently paid from any assets in my estate without respect to what is or is not included in the Marital Trust * * * [*Id.* at 619.]

Based upon the above election available to the executor, we concluded that the marital trust might be charged with those taxes and that the marital deduction was accordingly reduced. We distinguish that case on its facts.

The executor's choices in *Estate of Wycoff* were between two shares of the estate, the marital trust and the nonmarital trust, both of which were included in the gross estate, and not between principal and income, where only principal would be included in the gross

estate and income would be accounted for and taxed separately, as noted above.

We decline to read *Estate of Wycoff* more broadly to make the result depend entirely on the discretion of the executor. We will confine *Estate of Wycoff* to its facts and to the more narrow interpretation which we believe was intended by the Court.

Respondent cites Ga. Code Ann. section 53-2-101 (Michie 1982) as support for the contention that Georgia law requires expenses to be allocated to principal rather than income. However, that section only requires allocation of expenses to the principal if no other provisions are made by the will. Ga. Code Ann, section 53-15-3 (Michie 1982) allows decedents to grant their executors the power to allocate expenses between principal and income. Decedent, in this case, clearly granted such power to his executors.

Finally, we conclude that the settlement agreement did not alter decedent's grant of the power to allocate expenses. The settlement agreement merely set forth a formula for determining the final amounts of both income and principal to be received by Mrs. Hubert and the charity. That this is the case is demonstrated by the fact that both parties agree the marital portion, as calculated under the settlement agreement, should be reduced by income in order to determine the marital deduction. The fact that the settlement agreement provided for allocation of expenses between the marital and charitable portions does not preclude the executors from allocating those expenses to income rather than principal within those portions pursuant to the 1982 will.

Respondent cites a variety of cases in support of the contention that the marital and charitable deductions must be reduced by expenses. However, none of those cases is on point. They deal with situations in which the will made no provision for the allocation of expenses and, therefore, the statute controlled the allocation. Here, we clearly have a provision in the will which controls the allocation.

We hold that the allocation of petitioner's expenses to income was permitted by Georgia law, and the marital and charitable deductions are not reduced by expenses so allocated.

Imputed Income

The third issue we must decide is whether the marital and charitable portions must be discounted by 7 percent per annum to take into account income deemed to be earned by the residue.

The parties agree that the amounts of the marital and charitable deductions should be based on the date-of-death value of the residue. The parties also agree that the marital and charitable portions as determined by the settlement agreement must be reduced by accumulated income included in those portions to arrive at the date-of-death value of the principal which will constitute the deductible amounts. The parties disagree about the amount that should be subtracted as income. Petitioner contends that actual income figures should be used. Respondent argues that an imputed figure of 7 percent per annum should be used. We agree with petitioner.

Respondent argues that Georgia law requires us to impute income of 7 percent per annum to the marital and charitable portions and determine the deductions in that manner. Respondent relies on Ga. Code Ann. section 53-2-97 (Michie 1982), which states: "A general legacy usually bears interest after the expiration of 12 months from the death of the testator", and Ga. Code Ann. section 7-4-2 (Michie 1982), which established 7 percent per annum as the legal rate of interest where an interest rate is not established, as support for the imputed income argument. However, those sections are not controlling.

In this case, we are not charged with the task of determining the amounts of income the marital and charitable shares were required to receive. We are charged with determining what amount of the residue went to deductible administration expenses and marital and charitable bequests. In making that determination, we must look to the residue at the date of death. *Jackson v. United States* [64-1 USTC ¶ 12,221], 376 U.S. 503, 508 (1964).

At the time of decedent's death, the amount of the residue was a definitely determinable amount. Under the settlement agreement, that amount was divided among the marital and charitable portions, which included income to the date of settlement, and the administration expenses. Despite the agreement's complex language and respondent's contention that the agreement is much more complex, the result is, in fact, very simple. The entire residue is divided among three deductible portions, making the entire residue deductible no matter how much income was or should have been earned later.

The value of the corpus at the date of death is the value used in determining the deductions. Any use of income figures is merely to determine the amount of income allocated to each of the portions; for that determination, it is appropriate to use actual income figures. For our purposes, however, that determination is irrelevant, since the corpus allocated to each of the portions is deductible.

We hold that the marital and charitable portions should not be discounted 7 percent per annum for income deemed to be earned by the residue in order to arrive at the marital and charitable deductions. Date-of-death values should be used. If the parties need income figures for purposes of the Rule 155 computation, actual income figures should be used.

Decision will be entered under Rule 155.

Reviewed by the Court.

PARKER, SHIELDS, COHEN, SWIFT, JACOBS, GERBER, WRIGHT, PARR, WELLS, RUWE, WHALEN, COLVIN, CHIECHI, and LARO, JJ., agree with the majority opinion.

HAMBLEN, C.J., did not participate in the consideration of this opinion.

"APPENDIX B"

[¶ 12,944] *Estate of Frances Blow Allen, Deceased, Bank of Oklahoma, N.A. and R. Robert Huff, Co-Executors, Petitioner v. Commissioner,* CCH Dec. 49,346, 101 T.C. –, No. 23, October 20, 1993, Dkt. No. 309-91, opinion by Judge Tannenwald. [Appealable, barring stipulation to the contrary, to CA-10. – CCH.]

[*Code Sec. 2056*]

Estate tax: Martial deduction: Interest passing to surviving spouse: Administration expenses. – An estate was not required to reduce the marital share of a decedent's residuary trust by the amount of the estate's administration expenses in computing the estate's marital deduction where the income of the estate attributable to the nonmarital share of the trust was more than sufficient to absorb the administration expenses. The marital deduction was not reduced because of applicable state (Oklahoma) law mandated that, in the absence of any direction to the contrary in the decedent's will, administration expenses were to be charged to income. In addition, the provisions of the will and state law mandated that the marital deduction be maximized. Further, Reg. § 20.2056(b)-4(a) was not applicable because there was no "material limitation" upon the right of the surviving spouse to the income of the marital share where there was no direction nor other requirement that the income of the marital share of the trust be used to pay the administration expenses.

The decedent, a resident of Oklahoma, died testate in 1987. The decedent's will provided that the residue of her

estate was to fund a credit shelter trust and a marital trust for her husband. The credit shelter trust was to consist of so much of the residuary estate as would equal the federal estate tax unified credit in effect for the year of her death. The residue not required to fund the credit shelter trust was to fund the marital trust. The will stated that it was the decedent's intent that the whole of the marital trust shall qualify for the unlimited marital deduction.

The net income of both the marital and credit shelter trust was to be paid to the decedent's husband at least annually. On the death of the husband, the remaining corpus of the marital trust and the income from the period between the last distribution date and the date of the husband's death was to be added to the principal of the credit shelter trust. Upon the death of the husband, the credit shelter trust was to be disposed of for the benefit of the decedent's issue. In addition, the terms of the decedent's will directed the executors to pay all death taxes out of the credit shelter trust, as an expense of administration. Further, the trustees were given all powers, duties, and responsibilities authorized by the Oklahoma Trust Act. The executors were empowered to exercise their sole discretion as to whether to claim items either as income tax deductions or as death tax deductions, without making any adjustments as between income and principal of any trust or as between any beneficiaries by reason thereof.

The co-executors charged the administration expenses totaling $119,650 to the income generated by the estate and made an irrevocable election under Code Sec.

642(g) to deduct the expenses on the fiduciary income tax returns.

The sole issue before the Tax Court was whether administration expenses should reduce the amount of the marital deduction. The estate argued that the provisions of the decedent's will and Oklahoma Law mandated that the administration expenses be charged to income and, therefore, that Code Sec. 2056 and Reg. § 20.2056(b)-4(a) did not require the amount of the marital trust to be reduced by those expenses. In addition, the estate urged that the Tax Court to adhere to its position in *G. Street Est.*, 56 TCM 774, CCH Dec. 45,201(M), TC Memo. 1988-553, notwithstanding the reversal of that case by the U.S. Court of Appeals for the Sixth Circuit (*G. Street Est.*, CA-6, 92-2 USTC ¶ 60,112, 974 F2d 723). In the alternative, the estate argued that the decision of the Sixth Circuit in *Street* was factually distinguishable.

The IRS, on the other hand, asserted that the applicable estate tax statute and regulations required that the marital trust be reduced by the amount of the administration expenses in order to arrive at the allowable amount of the marital deduction.

The court held that the marital trust did not have to be reduced by the amount of the administration expenses. In so holding, the court determined that the instant case fell within the ambit of the decided cases where the marital deduction was not reduced by the amount of death taxes or administration expenses because it was clear that, under the provisions of the will and state law, such items were to be charged to the nonmarital share and not to the principal or income of the marital share.

This was so because Oklahoma law mandated that, in the absence of any direction to the contrary in the decedent's will, administration expenses were to be charged to income. In addition, the provisions of the will and state law mandated that the marital deduction be maximized. Further, the court concluded that Reg. § 20.2056(b)-4(a) was not controlling because there was no "material limitation" upon the right of the surviving spouse to the income of the marital trust where there was no direction nor other requirement that the income of the marital trust be used to pay the administration expenses.

The court distinguished the facts in the instant case from *Street*, because *Street* involved a single marital trust of the entire residue estate, whereas, in the instant case, the residue was divided into a marital and a nonmarital trust. Moreover, the estate income of the nonmarital credit shelter trust in the instant case was more than adequate to cover the administration expenses. **Back references: ¶ 7565.674 and 7565.73.**